Growth and Poverty Reduction in Mozambique: A Framework for Analysis

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Abstract

The Government of Madagascar has been seeking ways of promoting rapid economic growth and poverty reduction. This paper draws on a range of international experiences to help identify some of the key issues that need attention if these goals are to be met in a sustained way. Major conclusions are:

- Poverty reduction will not occur in Mozambique unless there is rapid economic growth. Government policies should focus on promoting and sustaining rapid growth.
- Rapid economic growth cannot occur in Mozambique without broad-based expansion in agriculture. Efforts to promote industrialization independently of a rapidly expanding agricultural base cannot be sustainable.
- Macroeconomic stability is indispensable for rapid economic growth. This requires attention to monetary and fiscal policies, exchange rate management, and debt management. Policy makers will need to ensure that the large inflows of foreign assistance do not continue to artificially overvalue the real exchange rate.
- The GoM should drastically reduce its development agenda in line with its capacity to implement *and* sustain policy reform.
- The Government of Mozambique should begin implementing an 'aid exit' strategy in order to focus the attention on the task of sustainable development.
- Finally, GoM officials need to fully grasp and respond to the implications of globalization for Mozambique's future growth and development. The challenges and opportunities need to be understood. Two areas of particular importance are budgeting and financial management.

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Determining the relationship in Africa between poverty alleviation and sustainable growth, and economic policy reforms via good governance, capacity building, and structural adjustment programs is a complex but critical task.

Ishrat Husain "The Challenge of Africa" 1996, p.29

1. Introduction

The Government of Mozambique (GoM) identifies rapid growth and poverty reduction as its principal long-term objectives (GoM 1999). In view of the country's history and current income status, these are the appropriate development goals. More importantly, given Mozambique's recent economic performance, these goals can be readily achieved so long as the GoM sustains growth-oriented policies.

There is no point repeating the key problems of low income, limited physical and human capital, and disruption that have been confronting the GoM and its supporters in the international community. Descriptions of what Mozambique experienced during the 1970s and 1980s and the recovery that has been occurring during the 1990s are well known and widely available (World Bank 1997).[1] That said, there needs to be some explicit recognition of the types of initiatives that have spurred Mozambique's recovery and their dynamic (and potentially adverse) implications. In strategic terms, three points are relevant. These are massive flows of foreign assistance, unprecedented levels of debt relief (under HIPC-II),[2] and a dramatic increase in donor attention. As the GoM pushes forward with its strategy for accelerated growth and poverty reduction, these conditioning factors need to be kept in mind. No such strategy can become sustainable (and Mozambique can never fully develop) if: (a) the present extreme degree of aid dependence continues; (b) the budget and balance of payments deficits persist; and (c) the donor community's agenda continues to dominate official thinking about the challenges and opportunities for growth and development.

If public policy is formulated with these points in mind, Mozambique has the opportunity to enjoy a substantial period of "catch-up" growth as it builds upon its comparative advantages in agriculture, fishing, electricity generation (for the Southern African power pool), entrepot services, and tourism. Other areas where the country's comparative costs are low by international standards will undoubtedly emerge as the economy grows and gains from many of the well-known benefits associated with the "expansion of the market,"; the increased economic supply of land; learning-by-doing; "learning-by-trading"; and "learning-by-reforming." These benefits will materialize so long as key policy makers recognize that catch-up growth does not mean leap-frog growth. Given Mozambique's existing (physical and human) resources and its present role within the world's system of trade, exchange, and finance, the economy will not develop without rapid growth in agriculture, the broad-based expansion of infrastructure, and steady improvements in health and education.

The purpose of this paper is to examine some of the literature that is relevant to the challenges facing Mozambican policy makers as they seek to devise a strategy to accelerate economic growth and sharply reduce poverty. The literature covers a range of experiences from Africa and beyond.

A large amount of relevant material is available. I have been selective, seeking to emphasize issues relevant to Mozambique's circumstances and potential.

Many new ideas about development strategies continue to appear. Experience shows that these need to be treated with caution. The field of economic development is littered with once novel approaches that donor agencies have tried and discarded. To help avoid this pattern, a much larger proportion of policy research is now being undertaken collaboratively with teams of African researchers. I spend some of Section 4 reporting the outcome of one such effort undertaken in five African countries. Conducted under the heading of "restarting and sustaining growth and development in Africa" (RSGD),[3] this research highlights many of the issues currently facing the GoM.

The essay is organized as follows. Section 2 discusses economic growth and poverty, and briefly describes how the two are related. Section 3 examines the determinants of growth and poverty. It focuses on some of the key policy initiatives that have been used to accelerate growth and reduce poverty. Section 4 describes strategies to promote growth and alleviate poverty, and suggests how Mozambique might build on the lessons of international experience to formulate and implement policies relevant to both areas. Section 5 discusses selected issues related to Mozambique's efforts to promote economic growth and alleviate poverty. Section 6 has concluding comments.

2. Economic Growth and Poverty Alleviation

Economic growth is conventionally defined as the rate of increase in per capita real income. Poverty occurs when individuals and groups have incomes that fall below $1 (or $2) per day in purchasing power parity terms (World Bank 1990, 1995).[4] First used as a poverty benchmark over two decades ago, the lower figure is now taken as an international measure of absolute poverty.

There is a large amount of literature on economic growth and poverty. Research on these topics continues on a broad front. This is entirely appropriate since both are multidimensional, intersect at a number of crucial levels, and are influenced by a variety of economic, social, technical, and political factors.[5] Moreover, since many issues related to each topic remain unresolved, especially in Africa, research is continuing. Reflecting this, the current *World Development Report 2000/1*, carries the title *Attacking Poverty*.[6] Even in draft form, this report has been highly controversial. It has been sharply criticized for its impractical recommendations.[7] It has also come under fire both within and outside the World Bank for failing to emphasize the fundamental role of rapid economic growth in poverty reduction.[8]

a. Economic Growth

Economic growth, like all economic processes, generates 'goods' (benefits) and 'bads' (costs). Many benefits of economic growth are now widely recognized. They include the greater capacity of a society to produce goods and services, expanded consumer choice, improved physical amenities, greater food security, broader educational opportunities, better health and nutrition, and enhanced physical and social mobility.[9] All of these changes have been closely associated with rising per capita real income (Gillis *et al.* 1996, Ch. 3).

Numerous costs associated with economic growth have also been identified. Indeed, some of the sharpest social criticism published in the nineteenth century highlighted the backwash effects of the rapid industrialization then underway in Europe.[10] The issues have been revived in modern times and the adverse changes that accompany economic expansion have been widely studied (Myrdal 1968, 1970; Seers 1972; Fishlow *et al.* 1978; enda 1990; Mishen 1993; Streeten 1994). Some of these changes include environmental degradation, the depletion of non-renewable resources, regional imbalances that promote rapid rural-urban migration and, especially in low-income countries, the proliferation of urban slums lacking basic social amenities and physical infrastructure. Other costs, particularly in Africa, have been the emergence of large numbers of poorly educated, low-income workers, detached from the land but unable to find employment in the formal, urban, economy (World Bank 1995). Most seriously affected among this group have been women who do not have access to the resources and opportunities that would improve their economic positions, enhance their security, and begin to overcome the conditions that transfer poverty and inequality across generations.

These and other developments, especially in the late 1960s and early 1970s, raised serious doubts about the very basis of post-WWII growth. Responding to the images created by Rachel Carson's *Silent Spring* (reprinted in 1994); Meadows *et al.'s* work on the limits to growth (1974); Ehrlich's population bomb (1975); Hardin's tragedy of the commons (1968); and Brown's lily pond in *The Twenty-Ninth Day* (1978), academics and practitioners began searching for alternative growth paths.[11] For a brief period, considerable interest emerged, largely within the academic community, about a "no-growth society."[12] Stimulated by Ward and Dubos' description of "only one world," increasing numbers of specialists turned their attention to the issue of sustainable development (Solow 1992; Taylor 1996; Vincent and Panayotou 1997; Sachs 1997a).[13] Although concepts of sustainability continue to be debated, the degree of urgency has increased with the attention given to global warming, habitat loss, and other environmental issues in the wake of the international conferences at Rio de Janeiro (1992) and Kyoto (1997). To these matters has been added the potential problems arising from looming water shortages in many heavily populated areas (Leslie 2000). Mozambique, as a member of the large and increasingly dessicated Zambezi River basin, faces a series of delicate regional negotiations in the years ahead because all upstream countries are determined to withdraw ever more water from the river.

It is crucial to recognize the adverse effects of economic growth and, where possible, take steps to counteract them. Yet, poor countries like Mozambique need to keep these issues in perspective. Economic development is impossible without sustained economic growth. Just one fact makes that point. The United Nation's widely publicized objective of cutting African poverty in half by 2015 will fail unless the growth of income accelerates to 7 percent per annum across the whole continent (UN 1999; Amoako 2000). Since Mozambique's recent aid-boosted growth rate has exceeded this figure, there is a solid chance that it can exceed the United Nation's targets. For that to happen, Mozambique's present growth rate will have to be sustained. Since only two African countries (Botswana and Mauritius) have managed such a task over an extended period, the challenge of maintaining high average rates of growth should not be underestimated.

Countries that have ignored the critical importance of rapid growth to economic development have paid a high price. Indeed, the costs in human suffering and wasted economic potential in countries that have not grown have far outstripped the costs incurred through rapid growth. The cases of South Korea and Zambia are illustrative. In 1965, Korea's per capita income measured in US dollars was well under one half of Zambia's.[14] Korea was widely seen as one of Asia's basket cases. By contrast, Zambia was the rising star of Southern Africa. As can be seen from the table below, the per capita income of Korea (measured in PPP terms) in 1998 was $12,270 while that of Zambia was $860. (The non-adjusted data show a similar gap.) That is, relative to Zambia's income, the average income in Korea increased by a factor of around 40 over a period of 33 years. The data showing trends in output per worker, growth in trade, and growth in agriculture simply reinforce the fact that Korea's economy has been highly dynamic while Zambia's has retrogressed in a number of substantive dimensions.

Table 1: Zambia and Korea–Selected Social Indicators

	Zambia	Korea
Expenditure on education (% GDP, 1996)	2.2	3.7
Expected years of schooling M/F (1995)	8/7	15/14
Population on less the $2/day (1993)	98%	0%
Urvan access to sanitation (1995)	66%	100%
Annual growth of consumption/capita (1980-1997)	-2%	7%
Life expectancy at birth (males, 1997)	43	69
Female adult illiteracy (1997)	33%	4%
Maternal mortality/100,000 (1995)	650	30
Food production (1989-1991=100, 1995-1997)	95.6	119.1
Size of economy (1998, billion USD)	3.2	370
GNP per capita (1993 PPP)	860	12,270
Elasticity of real income per worker (1980-1998)	3.32	0.32
Growth of trade per worker (1980-1998, annual average)	5.17	-0.21
Agricultural value-added per capita (annual average increase 1980-1998)	2.71	-0.28
Real output per 10 units of capital (1980-1998)	2.1	0.6

Source: *World Development Report 1999/2000* Selected World Development Indicators and World Bank CD-ROM *World Development Indicators* 2000

Since Zambia's natural resource base is inherently richer than Korea's (and its population pressure substantially lower), the fundamental difference in performance reflects the development strategies pursued. Korea chose to emphasize growth derived from promoting exports (Gillis *et al.* 1996:85). From the late 1960s onward, Zambia promoted import-substituting industrialization (McPherson 1980, 1995; Lewis and McPherson 1996; McPherson and Rakovski 1999).

Additionally, the countries differ in the manner in which they dealt with economic imbalances. When Korea encountered major economic difficulties in 1981 and 1998, its policy makers focused on how to foster adjustment rather than how to finance the imbalances. Following a major terms-of-trade shock in 1974/75, Zambia's government attempted to finance its (internal and external) imbalances rather than adjust (Lewis and McPherson 1994). Because of this choice, Zambia has not grown or developed. Moreover, as a result of the accumulation of debt and erosion of its productive base, Zambia now lacks the capacity to help the 85 percent of its population whose income is less than $1 per day and the 98 percent who income is less than $2 per day (World Bank 2000:Table 4:237).[15] To the extent that poverty has been ameliorated in Zambia, it has been largely the result of efforts by the international community. By contrast, in Korea the quality of health, education, and other social amenities has improved to levels that are consistent with those of a country within reach of developed country status, as demonstrated by the fact that Korea became a member of the OECD in 1996. Having grown rapidly, Korea has had the resources to take explicit steps to deal with poverty. Not having grown, Zambia has lacked the capacity to prevent poverty from worsening.[16]

The implication for Mozambique is clear. Rapid growth and development is possible even from seemingly desperate positions. As shown by Korea (and several other countries) the "convergence" of income is a meaningful concept for countries that are willing to take the measures needed to permanently alter their growth performance. The requirement, however, is effective economic management and policies that raise productivity, stimulate enterprise, and draw all Mozambicans into the development process.

b. Poverty Alleviation

The preceding example reinforces a key point: nothing can be gained in terms of poverty reduction over the medium or long-term without policies that foster and sustain rapid economic growth.[17] This does not disguise or diminish some of the negative effects of rapid growth. Yet, as the example of Korea shows, rapid economic growth has provided that nation with the resources to deal with those effects. Furthermore, in Zambia's case, the lack of growth (in fact, significant economic regression) has deprived that country of the resources needed to deal with poverty. The data in Table 1 are instructive, particularly when we recall where both countries started from in the mid-1960s.

The basic issue for any government seeking to reduce poverty is to determine what aspects of poverty will be relieved most efficiently through rapid growth and what aspects require direct government action. Development specialists generally accept that growth, though essential, is not enough, particularly when the initial distribution of productive resources is highly skewed and there are gender-based and regional barriers in access to markets and economic opportunities (World Bank 1996, 1997, 1999; Ferreira 1999; Killick and White 1999; Cornia and Telfer-Taiwainen 1999; United Nations 1999; Goldman 1999; Mellow 2000). Nonetheless, when a government decides to act in ways that address these constraints (so that it effectively levels the playing field), it has to ensure that it minimizes any negative repercussions of its interventions on growth and poverty.

Of course, the approach could be reversed, as the IMF has done, by shifting its focus to poverty reduction and growth strategies (IDS 2000; IMF 2000). The general idea is that to garner support from the Fund, a country has to propose a strategy that meets pre-determined poverty reduction targets, using policies that accelerate the rate of growth. In a country with Mozambique's history, such an approach has high downside risks. By emphasizing poverty reduction rather than growth, the GoM risks missing both targets. Zambia's case should add a note of caution. The Kaunda regime spent so many of the country's resources ostensibly to create a (state-run) system that would remove inequality and poverty that the economy's capacity for growth collapsed. Korea did the opposite. By focusing on rapid growth, it created the conditions that alleviated poverty.

These outcomes need to be stressed. Without question, poverty alleviation is a compelling social objective. But governments, particularly those with weak institutions and limited human capacity, cannot assume (and moreover should not presume) that their interventions will be effective.[18]

The main reason for this is that poverty is a multidimensional phenomenon and not all aspects can be dealt with directly or efficiently. This point emerges most clearly from the many poverty studies that have been supported by the World Bank. Some dimensions of poverty identified in those studies include:

- Consumption of less than $1 (recently raised to $2) per day in PPP terms,
- Limited (or lack of) access to safe water,
- Limited (or lack of) access to health services,
- A high proportion of children suffering from stunting,
- High infant and under-five mortality rates,
- Low life expectancy at birth relative to developed country comparators,
- Low primary school enrollment rates, and
- High adult illiteracy rates (World Bank 1995:Table 1).

The list could be readily extended. For example, the soon to be released World Development Report 2000/1 adds that the low income and low human development common to situations of widespread poverty reflect powerlessness and vulnerability.

Such a multidimensional characterization of poverty is fully consistent with A.K. Sen's 1995 (p. 15) view of poverty as "capacity deprivation." He, like the World Bank researchers, argued that income deprivation is only one of several aspects of poverty. Noting that income is instrumental in dealing with some poverty-related problems, Sen nonetheless, stated:

> It is important to see human beings not merely as recipients of income but as people attempting to live satisfactory lives and to see poverty not simply as low income but as the lack of real opportunities to have minimally adequate lives (p. 17).

While this is not controversial, the basic question for GoM policy makers is the relative emphasis they should give to poverty reduction. Even a cursory glance at the list of potential indicators suggests that unless strict limits are set the activities undertaken will soon overwhelm the government's capacity, notwithstanding the extravagant support currently being provided by the donor community. Historical experience, however, suggests that the GoM would be better advised to focus on economic growth, giving only limited direct attention to a few, highly selected dimensions of poverty.

c. Redistribution, Poverty and Growth

One problem facing developing countries such as Mozambique is that, while it is useful to identify the various dimensions of poverty and to highlight the range of benefits and costs of growth, there are few options that are both effective and feasible. This is (perhaps) one reason why the redistribution of income (or wealth) has had such appeal. It is action-oriented, relatively straightforward and “simple” to implement (especially following revolutions), populist, and by ostensibly soaking the rich appears to be getting at the heart of the poverty problem. Yet, redistribution of income and wealth, particularly radical redistribution, has yielded few short or even medium term benefits. Countries following this path have found that long periods have been required to overcome the disruption it creates and rebuild confidence with investors and the public more generally.[19]

All countries have found that the redistribution of income and wealth will not make those who are poor rich, or even much better off. Over the period 1987 to 1997, the PPP adjusted GDP per capita in Mozambique averaged $576. Radical redistribution of income under these circumstances would have simply equalized poverty (defined as income below $2 per day) throughout the country. Having achieved such redistribution, the GoM would still face the task of promoting equitable growth.[20] Throughout the twentieth century, even countries such as the Soviet Union, Cuba and China, which were ideologically committed to promoting growth and equity, equitable growth proved to be beyond the governments’ capacities. China, for example, forcibly redistributed land and other assets, thereby sharply reducing inequality. But, having done this, the government still confronted the problems of how to promote growth and alleviate poverty. Mozambique would face the same set of issues were it to radically redistribute assets.

Furthermore, radical redistribution of income and wealth has proven to be socially and economically disruptive. It provokes capital flight,[21] deters capital inflow, and leaves the government with the challenge of relying on state intervention to stimulate growth.[22] A study reviewing the record of bureaucrats in business demonstrated that, from a development perspective, state-managed commercial activity has been a major drag on growth and development (World Bank 1995). The same conclusion was derived earlier in a study of structural adjustment in OECD countries (OECD 1994). More importantly, the historical record now conclusively shows that governments have poor instincts in determining the future course of economic activity. The success of government involvement in Japan through MITI (the Ministry of International Trade and Industry) proved to be temporary. From the 1960s to the late 1980s, the Japanese government appeared to be highly adept at helping private enterprises to adjust to emerging economic opportunities. However, much of Japan’s sub-standard economic performance during the 1990s can be traced directly to the government’s unwillingness to promote adjustment in response to the implosion of the financial sector (Katz 1999).

Nonetheless, history also reveals that the option of foregoing all government redistributive action is not viable. Even Hong Kong, perhaps the closest modern example of *laissez faire* capitalism, has made large public investments in infrastructure, health and education. Provided against a background of rapid economic growth, these programs redistributed income and opportunities more broadly, thereby interrupting the intergenerational transfer of poverty.

For policy purposes, the issue is one of balance. With both extremes untenable, the issue for public policy is to determine the measures that will boost the economy's capacity for growth while making tangible progress in alleviating poverty. There is now much research on how this might be done. In the early 1970s, for example, this topic engaged large numbers of scholars at the World Bank. Their efforts culminated in the volume *Redistribution with Growth* (Chenery *et al.* 1974).

The main thrust of this study was for governments to ensure that some of the resources generated by rapid economic growth were used to alleviate poverty and improve welfare. Governments committed to such a strategy would seek a combination of policies and incentives to foster the activities needed to sustain rapid growth. Some of the dividend from growth would then be used to ensure that the positions of the most vulnerable members of society are improved. A practical demonstration of such a strategy has been the so-called "Asian miracle." For many commentators, the essence of that miracle has been "rapid growth with equity" (WINROCK 1991; World Bank 1993; Lindauer and Roemer 1994; Stiglitz 1996; AsDB 1998; Radelet and Sachs 1998a). A similar message has been emerging from the research on restarting and sustaining growth and development in Africa that is discussed in more detail below.

The lesson for Mozambique (and other African countries) is that government activities to alleviate poverty have to be undertaken in ways that do not undermine the country's productive capacity. Although some of the details of the strategy have changed over the years (for example, increased attention to gender issues), nothing has emerged over the last three decades to change the conclusion that redistributive polices can only be sustained from the dividend produced by growth. Whatever its other problems, the new World Development Report *Attacking Poverty* makes this point well. The specific goals of poverty reduction–empowerment (especially of women), improved security, and expanding opportunities (both in employment and in the market) are also seen as ways to sustain economic growth.

3. Determinants of Growth and Poverty

Economic growth is the result of three processes.[23] First, available resources are used more intensively. Second, existing resources are reallocated in ways that raise their productivity. Third, there is an increase in the supply of productive factors. In practice, all three occur simultaneously. Elements giving rise to these changes include movements in relative prices of factors and products; shifts in demand for final goods and services; variations in the supply of complementary factors, particularly managerial and technical skills; changes in competitive pressure; and innovations resulting from technical advances and organizational improvements. A further determinant is the overall degree of macroeconomic stability. This latter point cannot be overemphasized. Since the majority of productivity-enhancing technical change is embodied in new capital (including human capital), rapid sustained economic growth will only occur against a background of stability. As noted below, such a setting is indispensable if countries are to keep local investment "onshore" and eventually attract foreign investors of the type whose activities will enhance growth and development.

a. Determinants of Growth

Using Available Resources More Intensively: For economies that are at or close to full employment, there is little to be gained in terms of growth from using available productive resources more intensively. Nonetheless, developing countries, particularly those in Africa, with a long history of market repression, frequently have large amounts of excess physical capacity co-existing with high rates of unemployment. In technical terms, the economy is operating within its production possibility frontier. Numerous activities can be cited. Many of them can be found in the public sector, among state-owned enterprises (SOEs), and private enterprises that benefit from high rates of protection.

Within the government, the problem arises largely because of imbalances in the budget. Capital investment is frequently undertaken with no assurance that the recurrent resources will be provided to operate that capital at or near its installed capacity. This “recurrent cost problem” is symptomatic of inefficient budgeting procedures. Though widely studied across Africa for many years, it remains a persistent and largely unresolved deficiency in public budgeting (Heller 1979; Gray and Martens 1983; Heller and Aghelvi 1985; Peterson 1996).

Capacity underutilization in many SOEs reflects a broader set of influences. Some enterprises are so over-burdened with debt that they cannot raise the working capital needed to sustain their operations. Others have difficulty gaining access to foreign exchange to pay for the spare parts and raw materials to support their productive activities. Still others have managers whose personal goals and behavior are inconsistent with the efficient operations of the enterprise. Finally, even if SOEs are well managed, some will have underutilized capacity because of deficient domestic demand. Largely due to declining real per capita income associated with macroeconomic instability, deficient demand has created excess capacity in private enterprises as well. This phenomenon, widespread in Africa, has been referred to elsewhere as “running Adam Smith in reverse.” Declining per capita real demand leads to a contraction of the market and dissipates the unit cost advantages of specialization in production and the division of labor (Duesenberry, Goldsmith and McPherson 1999).[24]

Raising the Productivity of Existing Factors: Governments can take numerous steps to raise the productivity of existing factors of production. Short-term measures typically focus on the setting within which the factors are used. These include removing restrictions and regulations (such as price controls), streamlining customs procedures to reduce the costs of importing complementary inputs, repairing and/or rebuilding key infrastructure, and avoiding policy actions that undermine confidence or destabilize the economy.

Over the longer term, enhancing productivity will involve education and training, improvements in health, less costly transport and logistics (including information transfer), and good governance (notably the security of property, enforcement of contracts, impartiality of the legal system, and control over corruption). Macroeconomic stability is also essential to encourage entrepreneurs to invest in new technology. Movements in the real exchange rate–the relative price of tradable goods and services (G&S) to non-tradable G&S–is crucial in this respect. If the real exchange rate remains overvalued, entrepreneurs will be induced to reallocate their resources in ways that are inconsistent with the country's dynamic comparative.[25] In particular, they will seek ways to minimize their cost disadvantage by engaging in short-term ventures (trade and inventory accumulation), or moving their resources abroad.

Increasing the Supply of Productive Factors: Investment adds to productive capacity leading, in turn, to a larger output of G&S. (Our earlier discussion also noted that higher rates of investment provide countries with the capacity to address some of the adverse effects of economic growth.) Some productive factors, such as machinery and equipment, can be accumulated relatively quickly. Other factors, such as skilled personnel and fundamental research and development, take long periods to emerge and add to output. This has been especially true in Africa where the general level of human capital needed to sustain rapid growth in a competitive international setting has been low. Many African governments have made extraordinary efforts to expand training and education thereby boosting the human capacity needed to support sustained growth (Grindle, Mann and Shipton 1989; World Bank 1991; Kelley 1991; Psacharaopoulous 1994; Grindle 1997; ADB 1998; Hoover and McPherson 1999). Because this task is time consuming, specialists have sought methods for shortening the process. Research over the last decade and a half has stressed the capacity-building advantages of both trade and growth.[26] "Learning-by-doing" is the classic case and accounts for large amount of technical assistance designed to replace itself with local capacity. More recent efforts have emphasized the advantages of "learning-by-trading" and "learning-by-reforming." An important dimension of the latter process has been the lessons that African countries can learn from Asia's development experience (WINROCK 1991; World Bank 1993; Lindauer and Roemer 1994).

A number of elements are needed for a country to invest at a rate that raises the growth of its productive capacity. These include mechanisms to efficiently mobilize and reallocate savings, a legal and regulatory framework that induces entrepreneurs to invest (i.e., incur current costs in the expectation of future returns), and the prospect of expanding markets to support the derived demand for capital.

Since investment is long-lived and significant parts of it are irreversible (or reversible only at high cost), investors need to be assured that the conditions inducing them to commit their resources will remain in place over the long term. Development specialists have come to understand that irreversibility and option values are critical factors in determining investment decisions (Pindyck 1991; Hubbard 1994; Severn 1996; Cuddington, Liang and Lu 1996; Collier and Patillo 2000). Under conditions of heightened uncertainty (such as those accompanying macroeconomic instability) potential investors will exercise the option of waiting. This option involves an opportunity cost because it delays completion of, and therefore postpones the rewards derived from, specific activities. Nonetheless, it also has the advantage for investors of providing the flexibility to make the investment at a later date should conditions improve. For an individual, the option of waiting is a rational response to uncertainty. For any government seeking to raise the rate of investment so as to accelerate economic growth, having large numbers of investors decide to wait can have devastating consequences.

The implication for the GoM is clear. In order to encourage private investors (local and foreign), it needs to create and maintain a stable, predictable setting that offers the prospects of expanding markets and expected returns consistent with the risks that investors are incurring. While I do not dwell on aspects of governance in this essay, one of the essential features of a predictable setting, needed to encourage long-term investment, is open, transparent, and accountable activities by the government and its agencies. On this point, Mozambique's reputation (externally at least) is poor. A recent report by Transparency International ranked Mozambique (along with Nigeria, Cameroon, Kenya, and Angola) as the most corrupt settings for business in Africa.[27] This is not flattering company for any country that aspires to long term growth and poverty reduction. Even if even the report is only partially true, it confirms that the last decade of growth has little foundation other than massive donor transfers. Removal or reduction of those transfers would leave little to sustain productive investment.

b. Alleviating Poverty

Government actions have direct and indirect effects on poverty. Direct effects involve programs that target *and* actually reach the poor. Indirect effects operate through policies that stimulate growth in sectors (such as agriculture and the informal urban sector) from which the poor derive their livelihoods.

The government budget allocates resources among productive factors, distributes expenditure over activities, and redistributes income (and wealth) through transfers and taxes. The efficiency with which the government carries out its operations provides a foundation for all economic activity. For government expenditure to reduce poverty on a sustained basis, the national resource base has to expand. That cannot occur in the face of gross inefficiency in public budgeting (Easterly and Schmidt-Hebbell 1993; McKenzie *et al.* 1996).

Government efforts to reduce poverty fall into two categories. The first category is targeted programs that seek to distribute income or physical products directly to specific groups who have been identified as poor. The second is the general provision of services such as education or health, or the expansion of infrastructure, the services of which raise the welfare of the poor.

The rationale for the first set of activities is that government action can directly address specific dimensions of poverty. An example is the distribution of food or seed to farmers in drought or flood affected areas. However, targeting raises two common policy problems, the (so-called) F and E mistakes (DPMN 1993; Cornia and Stewart 1995:351; D. van de Walle 1995; and Warr 2000). The F-mistake is the failure to reach the target population (i.e., the policy is ineffective). E-mistakes occur when the intervention reaches the non-targeted population (i.e., the policy is inefficient). Both mistakes raise the costs of alleviating poverty.[28]

The rationale for the second set of activities is that the general improvement of amenities has positive spillover effects, thereby raising the overall level of social welfare. The idea is that "a rising tide lifts all boats."[29] A number of well-known measures are included in these activities: universal primary education, preventive health care (particularly immunizations), water treatment facilities to reduce water-borne diseases, national food reserves to counteract famine, "sites and services" projects to improve conditions in urban slums, and rural electrification. All of these are public goods.

Another public good is reduced inequality. A high degree of income inequality is a major barrier in efforts to reduce poverty, largely because it skews the growth process in ways that disadvantage the poor (Chenery *et al.* 1974; Lipton 1977; Meier 1984; Marris 1999; Cornia and Telfer-Taivainen 1999; Gugerty and Timmer 1999; Ali and Elbadawi 1999; Barro 1999; World Bank 2000:Ch. 4; and Mellor 2000). Actions that reduce "social distance," i.e., lower inequality, have been shown to ease social tensions and provide a foundation for more rapid, sustained growth. In policy terms, the challenge is to devise programs that induce those who control the majority of income and wealth in the society to behave in ways that make growth more inclusive. Changes underway in Latin America have been instructive. Despite their high degree of inequality, countries such as Chile and Argentina have been using the fruits of rapid growth to address the problem of inequality in ways that boost growth and reduce poverty (Lustig and Arias 2000). Three such measures have been to cut government subsidies (which typically benefit the well-to-do), improve tax administration (so that those with higher incomes bear a fairer share of the burden of public expenditure), and sell public enterprises (whose operations are frequently captive to special interest groups). In Africa, Mauritius provides an example of a country that has grown rapidly and sharply reduced poverty. Data from 1996 show that the number of people in poverty (based on the *national* poverty level) was 11 percent of the population. None of that population was below the international daily poverty standard of $2 in PPP terms.[30] Growth and poverty reduction was achieved in Mauritius without only a minor worsening of the income distribution. Over the period 1980 to 1991, the annual growth rate of the incomes of the lowest 20 percent of the income distribution was 3.2 percent while the overall growth rate of per capita income was 3.7 percent. The outcome was that the income share of the bottom 20 percent declined from 7.1 to 6.7 percent (Gallup, Radelet and Warner 1999:2).[31]

c. Growth, Poverty and Inequality–The Evidence

It will become evident as the discussion proceeds that a more appropriate title for this section should be "growth, poverty, and inequality–the controversy." The compilation of large cross-country databases on income inequality by researchers at the World Bank has allowed scholars to examine in greater statistical detail the links among growth, poverty, and inequality (Deininger and Squire 1996). Since all of these concepts are multi-dimensional, relationships among them are likely to be complex and difficult to disentangle. This has been verified in practice. Some major concerns have included:

- Does inequality worsen under conditions of rapid growth?
- Does extreme inequality hinder growth?
- Does rapid growth alleviate poverty even if inequality increases?
- How does food insecurity (as a key dimension of poverty) affect growth?
- Do existing coping strategies undermine attempts to accelerate the rate of economic growth?

All of these questions are relevant to the goals being pursued by the GoM. They all reflect the idea that there is an important trade-off between rapid growth, inequality, and ultimately sustained poverty reduction. All governments face the question of whether they should emphasize growth with the expectation that it will reduce poverty and inequality, or whether they should focus be on poverty reduction with the expectation that this will raise the rate of growth. Although the IMF appears to have fudged this issue by introducing its "poverty reduction and growth strategy" (PR&G), countries that have to formulate and implement such a strategy should recognize the difficulties. For example, it has already been noted that no developing country has successfully implemented a PR&G strategy along the lines proposed by the IMF (IDS 2000). Given the history of the Enhanced Structural Adjustment Facility (ESAF), which the PR&G strategy has replaced, successful implementation will not be easy. More important, no country (developed and newly industrialized) has made the transition to higher income levels in ways that have avoided such a trade-off.

Thus, for the GoM, the relative emphasis it should give to growth or poverty reduction is not a trivial or incidental issue. There are no easy answers for making that choice. This is why I noted that 'controversy' was a more appropriate term. In particular, there are no prescriptions of the type: if the initial income distribution is *x* and the growth rate is *y*, then poverty will fall by *z* over a period of years. Nonetheless, some broader lessons have emerged. One such lesson is that sustained poverty reduction is impossible without sustained economic growth. It was once believed that Sri Lanka and Cuba were counter-examples. Both countries had important early success in reducing poverty even though their growth rates were low. But, lacking sustained growth, the progress they made in reducing poverty did not endure. Another lesson is that, apart from the special cases of city-states such as Hong Kong and Singapore, rapid sustained growth has not occurred in any country without broad-based improvements in agricultural productivity.[32] Furthermore, despite the enthusiasm with which manufactured exports are proposed by some specialists, their expansion has not proved to be an adequate source of sustained growth in the absence of an expanding agricultural base.[33]

A third lesson is that trade cannot support rapid growth and poverty reduction unless the major imbalances in the domestic economy are also removed. A high-level example is Japan. Despite its impressive trade performance and large balance of payments surpluses, the country as a whole has experienced a decade-long domestic slump largely due to the persistent distortions in its financial system (Katz 1999). A low-level example has been Madagascar. During the 1990s, its manufactured exports grew by 15.3 percent per year while overall real GDP increased by only 0.7 percent per year (African Development Indicators 1998/99:Tables 2.1, 5.34).

The links among growth, poverty, and inequality have been widely examined. None of the key issues involved is particularly new. They have been studied from a variety of perspectives ever since Kuznets hypothesized in the mid-1950s that income distribution systematically worsens during periods of rapid growth. However, what is new is the breadth and richness of the empirical analysis of those links. With more detailed data now available, scholars have been able to test a variety of propositions that were formerly matters of conjecture. This work has generated considerable controversy. For instance, Krugman (1994) acknowledged that many countries in East Asia had made major progress in reducing poverty through rapid growth. He did not believe that the growth was sustainable, comparing what had been achieved in Asia to the rapid growth achieved in the socialist systems during their years of forced-pace capital accumulation. Radelet and Sachs (1998) challenged that view by citing evidence that the "Asian miracle" was not just a product of rapid capital accumulation but also involved significant improvements in productivity.

In other work, Bruno, Ravaillon and Squire (1996) examined a large set of cross-country data to show that empirical evidence was weak for the Kuznets hypothesis. They reported time series regressions suggesting that there had been no discernible trend over time in the Gini coefficients in a large number of countries. They concluded that both developed and developing countries have grown, in some cases at high rates, without a noticeable worsening of the income distribution.

Studies conducted under the USAID-funded Consulting Assistance for Economic Reform (CAER-II) project have extended that analysis (Roemer and Gugerty 1997; Gallup, Radelet and Warner 1999; Gugerty and Timmer 1999). For instance, Roemer and Gugerty (p. 14) found that "…economic growth benefits the poor in almost all countries in which substantial growth takes place." Though the connections are complicated, their evidence shows that open economies have been more successful at reducing poverty than countries that close themselves off from international trade and exchange. Gallup, Radelet and Warner (GRW) report similar findings. Basing their analysis on the Deininger and Squire data referred to earlier, they showed that the incomes of the poorest groups grow, on average, at rates similar to the incomes of the richest members of society. Specifically, their evidence points to what they call a "one-to-one" relationship between the income growth of the poorest groups and overall income growth. The same result was later reported, without acknowledgment, by Dollar and Kraay (2000). However, both of these studies played down a major anomaly that exists in the case of China. Evidence shows that income growth of the lowest quintile has not been "one-to-one," being more than 2 percentage points lower than the average growth of income (Gallup, Radelet and Warner). Since the number of people involved (250 million) is large by any standard, this is a major gap in the argument. Rather than attempt an explanation, GRW skirted the point to emphasize the broader result that growth does not necessarily hurt the poor.[34]

By contrast, Timmer and Gugerty found that growth has not benefited the poorest groups, especially in countries where the bias of government policies has been anti-rural and anti-agriculture. Their results illustrate in ways not brought out by GRW.[35] that the initial distribution of income and wealth and the sectoral composition of growth make a significant difference to the subsequent income growth of the poor. What Timmer and Gugerty have established is fully consistent with the body of research on rural growth linkages first undertaken by Mellor in 1966 and 1976 and continued to the present day by scholars at the International Food Policy Research Institute (Delgado 1995; Badiane and Delgado 1995; Delgado *et al.* 1998; Barrett and Carter 1999).

In a recent study, Goldman (1999) underscored the importance of agriculture and food in strategies to promote growth and improve distribution. His analysis intentionally steps back from the distribution of income (and wealth) to consider the distribution of food (calories). Goldman treats this as an index of "food poverty." On a worldwide basis, the data he assembled show that the distribution of food is highly unequal. Nonetheless, with the exception of sub-Saharan Africa, food supplies and average levels of food consumption have risen over time. Goldman examined a variety of schemes to improve the distribution of food, concluding (like many before him) that the most effective way of reaching the poor was through agricultural and rural development. Goldman, however, doubted that the ultra-poor, whose positions are highly marginal even in the rural sector, could be reached without special programs. He maintained that sustained improvements in the food security (and by extension, the income) of this group would require some form of public support.

A further concern, particularly in countries that have plans to sharply accelerate the rate of growth, is the problem of drawing the very poor into the growth process. Much has been written about the problems of "trickle-down" growth. Some countries, e.g., Burkina Faso and Malawi, have even been urged to push for "trickle-up growth" (Rotberg *et al.* 1994; Roemer *et al.* 1996). Moving beyond the slogans, there is a special need to be concerned that the coping strategies adopted by the very poor may block their ability to take advantage of new opportunities for income generation.

Highly conservative strategies have been adopted by the poor as a means of limiting their downside risks. When closely analyzed, such strategies reflect "safety first" criteria. Since nothing in life is fail-safe, the very poor tend to follow "safe-fail" approaches. That is, they develop patterns of behavior so that, in the event of an adverse shock, they can avoid complete destitution. Given that the poor have few resources and their circumstances provide few opportunities for augmenting those resources, obtaining such protection from adversity is difficult. Nonetheless, they try, and many variants of coping strategies have been observed among the poor in both the rural and urban areas.[36]

The basic idea of such a strategy is that under "normal" circumstances, it provides a "floor" to the income or consumption of a family unit. However, a widespread problem in Africa is that general economic conditions have continually deteriorated. An example is Zambia, where from 1972 to 1991 real per capita income declined by 50 percent, and from 1992 to 1999, income fell 30 percent (Hill and McPherson). Though Zambia's experience is somewhat extreme, declining income and collapsing economic activity is not unusual across sub-Saharan Africa. Until the early 1990s, the experience in Mozambique was similar. Situations such as these severely test the strategies that the poor use to defend themselves from economic stress. Drawing on a much broader view of the African situation, World Bank researchers (1995:3) observed that poverty was being aggravated by insecurity. They noted:

> Because of the economic crisis [in Africa] and decreased job opportunities, self-employment has become the most promising income-generating activity. However, self-employment is associated with unstable and unsafe working conditions, low wages, temporary status, clandestine activities, and the absence of labor legislation coverage. Coping strategies of the traditional culture appear to be breaking down. Family and neighborhood patterns of solidarity no longer prevail. Many unmarried women are forced to make a living for themselves and their children in a hostile environment of crime, political unrest, and the AIDS epidemic.

For policy makers, the prevalence of coping strategies raises a number of important issues. The first is that, because of their nature, such strategies will not be discarded or abandoned readily.

Economic conditions will need to improve over a long period before the very poor will feel safe enough to begin assuming additional risks. A second point is that without explicit action that effectively raises the welfare of the very poor, they will be left behind as growth accelerates. The coping strategies that prevent the poor from complete destitution also hinder them from responding rapidly to economic opportunities of which those with more wealth (and lower aversion to risk) can take advantage.

A third point is that for the very poor it is more important to make steady progress with the minimum chance of a set back than rapid progress that has high risks of a major setback. Killick and White (1999:3)) stressed this point when they argued that government programs to promote growth should explicitly avoid actions that increase the pressure on the poor. They specifically noted that policy makers "need to focus on reducing shocks and helping the poor smooth the shocks." A fourth point is that actions designed to help the poor change from a strategy of merely coping cannot succeed unless the links between gender and poverty are directly addressed. Many coping activities fall to women. Much of the recent discussion regarding "inclusion" and "empowerment" is an explicit recognition of this fact.

The World Bank study *Attaching Poverty* (referred to earlier) attempts to summarize the evidence on the relationships between growth, poverty and inequality (p. 25). Its overview of the literature confirms the complexity of the relationships and highlights the broad variety of country experiences. Some rapidly growing countries such as China have experienced a reduction in poverty but (as noted above) an increase in inequality. Some countries, like Zambia, that have had no growth, have experienced sharp increases in poverty. The situation has been further complicated by the financial turmoil in Asia during 1997 and 1998 that reversed some of the earlier gains in poverty reduction. Subsequent political developments have exacerbated the problems of income insecurity and vulnerability, particularly in Indonesia and Thailand. Reviving concerns that were common during the 1960s and early 1970s, the International Labor Organization in its recent *World Employment Report* (ILO 1999) noted that the loss of employment in the wake of the Asian crisis (and crises in Russia and Brazil) has adversely affected incomes and general economic welfare. A major concern has been the expanding group of young people with few qualifications who are unable to find productive work.

Overall, the evidence underscores the importance of sustained economic growth and macroeconomic stability if countries are to make major progress in alleviating poverty. The "new" wrinkle in the World Bank report is the emphasis given to broad-based programs of empowerment, security, and opportunity. For governments impressed by its messages (or those that are pressured by the donors to implement its key findings) the main policy challenge will be to design activities that enhance participation by the poor, improve their overall security (as measured by income and assets), and expand their opportunities for productive employment. There are numerous suggestions how these tasks might be accomplished. As already emphasized above, the main problem for Mozambique is that the agenda for attacking poverty requires more capacity (institutional, financial, and human) than is available. The agenda also implies a continuing heavy dependence on foreign assistance. Such dependence may lead to a temporary reduction in poverty but, as aid is currently dispensed and used, it will not lead to sustained economic growth.

d. Growth and Poverty in Mozambique

The data in Table 2 together and the information in the World Bank's "Mozambique at a glance" (inserted) provide a detailed overview of trends in the macro economy. Though categorized by a reviewer of an early draft of this essay as 'stale,' the data highlight many of the key issues relevant to the formulation and implementation of growth and poverty alleviation strategy.[37] Table 2, derived from the World Bank's *World Development Indicators,* has selected macroeconomic indicators over the period 1980 to 1997. Although some more recent data can be obtained from World Bank and IMF web sites, data on some of the key macroeconomic variables are lagging. I have been informed that keeping abreast of the data is a matter that is being seriously addressed by the GoM. Experience elsewhere in Africa shows that this is an area that requires constant attention. Up-to-date data that are readily available to policy makers, the general public and potential investors are essential if the GoM is to move beyond guesswork in its attempts to accelerate growth and alleviate poverty. No country has ever successfully managed its macro economy using data that are not current. Mozambique will not be the first.

The data show some impressive gains in real GDP from 1987 onwards. Since a large part of that growth has resulted from the restoration of peace and subsequent reconstruction, the policy challenge is to establish policies and institutions that allow the economy to sustain the momentum. Real per capita incomes have also risen. Notwithstanding this positive change, real incomes are low by international standards. This simply reinforces the need for continued rapid economic growth and the urgency of feasible and sustainable actions to alleviate poverty.

Agriculture represents between 30 and 40 percent of GDP. This provides Mozambique with an important opportunity to use agriculture as a base for simultaneously raising the rate of growth *and* alleviating poverty. That, however, will require the GoM to make agricultural growth the highest priority on its development agenda.

The data on exports and imports and gross domestic savings and gross domestic investment point to two major gaps in the economy. Imports are orders of magnitude greater than exports. Correspondingly, domestic investment is orders of magnitude greater than domestic savings. The gap between exports and imports has been closed through foreign borrowing and foreign aid.

Table 2. Mozambique: Selected Macroeconomic Indicators, 1980-97

	1980	**1981**	**1982**	**1983**	**1984**	**1985**	**1986**	**1987**	**1988**	**1989**	**1990**	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**
GDP growth (annual %)	..	5.0	-6.9	-15.7	-6.5	1.0	-2.3	14.7	8.2	6.5	1.0	4.9	-8.2	8.6	7.5	4.3	7.1	11.3
GDP growth per capita (ann. %)	..	2.3	-9.5	-18.1	-8.6	-0.6	-3.5	13.7	7.4	5.8	0.2	3.0	-10.0	6.5	4.8	1.7	4.5	8.8
GDP (bill. 1995 USD)	1.6	1.7	1.6	1.3	1.3	1.3	1.2	1.4	1.5	1.6	1.6	1.7	1.6	1.7	1.9	1.9	2.1	2.3
Population growth	2.8	2.7	2.6	2.4	2.1	1.6	1.2	1.0	0.8	0.7	0.8	1.9	1.9	2.1	2.8	2.6	2.6	2.5
GDP per capita (1995 USD)	134.4	137.4	124.6	102.6	94.0	93.4	90.2	102.4	110.0	116.3	116.6	120.0	108.2	115.1	120.4	122.4	127.8	140.2
GDP per capita (PPP, int'l dollars)	410	440	400	330	320	340	350	440	500	520	530	560	530	580	620	640	680	740
Agriculture, v. a. (% of GDP)	37.4	35.9	40.6	32.4	30.2	47.5	41.1	44.1	42.9	47.4	44.5	37.1	33.7	32.0	29.5	30.2	31.5	31.0
Exports of G&S (% of GDP)	15.0	13.8	11.5	8.5	5.7	4.0	3.5	9.2	11.2	11.4	11.3	15.5	19.2	18.3	19.4	21.0	20.8	18.2
Imports of G&S (% of GDP)	31.8	29.9	30.5	26.5	21.3	13.3	14.0	36.5	43.4	44.9	41.9	44.7	54.3	56.3	55.4	46.4	41.5	34.1
Inflation, CPI (annual %)	..	..	..	..	..	..	..	..	50.1	40.1	47.0	32.9	45.5	42.2	63.2	54.4	45.0	5.5
GDS (% of GDP)	-8.4	-7.8	-10.5	-10.5	-7.4	-3.1	-3.5	-10.4	-10.9	-12.7	-8.7	-6.7	-8.0	-11.4	-4.8	10.6	9.4	13.6
GDI (% of GDP)	8.3	8.4	8.5	7.5	8.2	6.3	7.0	16.9	21.3	20.8	21.9	22.5	27.1	26.5	31.3	36.1	30.1	29.5
Net ODA and official aid (mill. USD)	169.2	143.5	207.8	210.5	306.0	369.8	572.4	769.5	994.3	887.0	1078.9	1104.6	1474.2	1183.3	1231.4	1101.4	923.0	963.2
Ex. rate (Meticais per USD, p. a.)	32.4	35.3	37.8	40.2	42.4	43.2	40.4	290.7	524.6	744.9	929.1	1434.5	2516.6	3874.2	6038.6	9024.3	11293.8	11543.
CPI (1995=100)	..	..	..	..	..	1.3	..	4.7	7	9.8	14.4	19.2	27.9	39.7	64.8	100	145	153
Real Ex. Rate *	..	..	..	..	..	2747	..	5097	6423	6841	6013.3	6978.1	8469.7	9300	8993	9024	7968	7718
External Debt (bill. USD)	0.05	..	..	..	..	2.87	3.49	4.13	4.16	4.36	4.65	4.72	5.13	5.19	5.62	5.73	5.78	5.99

Note: * Calculated as nominal exchange rate times the ratio of the US PPI to the domestic CPI.

Sources: World Development Indicators, 1999, World Bank

International Financial Statistics, March 2000, IMF

These resource flows have been huge both in absolute terms and relative to the size of the Mozambican economy. Such a situation is not sustainable even over the medium term.[38]

The recent need for HIPC-II debt relief for Mozambique is tangible evidence that the government's strategy of using foreign borrowing to fill the gap between imports and exports was counterproductive. The implication, now known to all foreign creditors, is that Mozambique did not use the foreign loans efficiently or effectively. While the present government may insist that circumstances have changed, foreign creditors are likely to remain skeptical. Accordingly, further foreign borrowing is not a viable option for dealing with the external imbalance. Much the same can be said about the option of continuing to rely on foreign assistance. Undoubtedly foreign aid has been essential in helping to jump-start reconstruction and rationalizing Mozambique's foreign debt.

A key issue facing the GoM is how much more the country should rely on foreign assistance. As I note below, foreign assistance is a two-edged sword. If used appropriately, it can add to the nation's productive capacity. On the other hand, foreign aid imposes a number of burdens on any country. Not the least is the pattern of dependency (reflected in the behavioral and organizational changes within the government itself) that for almost all African countries has proven to be too convenient and too difficult to unravel.

If foreign assistance is not to continue filling the gap between imports and exports in the foreseeable future, there are two options. The first is the introduction of policy changes that restrain imports to the level of exports. The most obvious of these would be a (much needed) major devaluation of the real exchange rate.[39] The second is that domestic savings (still exceedingly low) will have to increase. Indeed, the only viable strategy for Mozambique to grow rapidly and alleviate poverty on a sustainable basis is for domestic savings to rise as overall reliance of foreign assistance declines.

The data reported in "Mozambique at a glance" (version 8/31/00) confirm the above trends. One commendable recent change has been the sharp reduction in the rate of inflation. While policy makers have reason to welcome this news, they need to recognize its source. Massive foreign assistance has eliminated the "need" for domestic bank financing of the budget (i.e., money creation) even though tax effort is low. Furthermore, international inflation has been at its lowest rate since the early 1960s. Because it is so heavily dependent on imports, Mozambique has been "importing" price stability. For policy makers, an important question is whether they can sustain the domestic budget and monetary conditions needed to keep inflation low in the face of external price shocks (e.g., in oil prices and transport costs) and an eventual reduction in foreign financing.

The basic social indicators for Mozambique, though improving, are generally poor by international standards. Mozambique's recorded infant mortality rate of 134 per 1000 over the period 1993 to 1999 is high relative to the rest of Sub-Saharan Africa and much higher than all low-income countries. Other indicators – illiteracy, access to safe water, life expectancy, female enrolment in schools, and income levels – underscore the extent of catching-up that needs to be done. An important lesson from other countries and regions is that if the appropriate measures are adopted, the catching-up can occur rapidly. Where Mozambique has an advantage is that it is growing rapidly, its debt burden has been significantly reduced, and exports have been growing rapidly. The latter, however, has been inadequate to reduce the balance of payments deficit. Indeed, the adverse trend in this datum should be a major source of concern for policy makers. Its persistence will block growth and poverty reduction over the medium and long term.

4. Strategies for Promoting Growth and Poverty Reduction

How do growth and poverty alleviation strategies overlap? In what ways are they complementary? Recent research by U.S.-based and African scholars provides some guidance. Conducted as part of a joint effort to understand how to restart and sustain growth and development in Africa, the research builds upon the comparative experience both inside and outside Africa as well as insights gained from detailed studies of Ghana, Kenya, Senegal, Tanzania, and Uganda. It shows that activities needed to restart and sustain growth and development (of which poverty reduction is a key element) include the following (Duesenberry, Goldsmith, and McPherson 1999; McPherson 2000):

- achieve and maintain macroeconomic stability,
- stimulate growth in agriculture (and other selected productive sectors),
- reform the public sector in ways that sharply scales back the development agenda to match the government's financial and administrative capacities,
- formulate and begin implementing an 'aid exit' strategy, and
- adopt a constructive approach to the globalization of economic activity.

We examine each point in turn.

a. Macroeconomic Stability

The evidence that sustained economic growth will not (and cannot) occur in Africa (or any where else) while economies remain unstable is overwhelming.[40] Instability deters local investors and convinces potential foreign investors that their resources could be more productively employed elsewhere.

These propositions have been widely confirmed in cross-country regression analyses. Research undertaken by Calamitsis, Basu and Ghura (1999, henceforth CBG) is illustrative. Based on data drawn from 32 African countries for the period 1981 to 1997, CBG show that:

- some African countries are "on the move";
- the overall economic and social situation remains "fragile";
- the challenge for policy is to maintain the momentum of reform, focus on growth and poverty alleviation, and ensure that Africa "integrate[s] itself fully into the world economy."

CBG derive their empirical results from a single equation that regresses the growth in per capita real income on the initial income level, population growth, the ratios of private and government investment to GDP, an index of human capital, a dummy for how long IMF programs are sustained, the rate of inflation, the standard deviation of inflation, the central government budget deficit (excluding grants), the change in the real effective exchange rate, the rate of growth of exports, the percentage change in external terms of trade, an index of political freedom, and dummies that account for wars and specific country and time effects. CBG explain the mix of empiricism and theory underlying their choice of variables. What they fail to explain, however, is why particular variables were excluded. This is a major weakness in their analysis.[41]

The results they report show that:

- private investment is strongly related to the growth of real per capita income;
- government investment is not an important determinant of real income growth (McKenzie *et al.* 1996 and Easterly 1999);
- human capital has a positive effect on per capita real income growth, but the effect is not robust;
- population growth has a major negative effect on real per capita income growth;[42]
- the coefficients on the budget deficit and the real exchange rate are negative and statistically significant;
- export growth is positive and statistically significant;[43]
- inflation is not highly statistically significant;[44] and
- sustained implementation of IMF programs have had a positive effect on growth.[45]

Though there are some qualifications, these results are consistent with other empirical research. CBG have focused on some of the key economic relations essential to macroeconomic stability. They show that higher, more stable rates of income growth in Africa have depended upon low budget deficits, low inflation, the expansion of exports, higher rates of private (not government) investment, and sustained economic reform. None of these results is controversial. Rather, they add to the overwhelming weight of evidence that efforts to achieve and sustain macroeconomic stability cannot be fudged if economic growth is to revive across Africa.

A result directly applicable to Mozambique is that a high rate of population growth has undermined the capacity for sustained growth. This result, which has been widely observed in similar work on Africa, strongly suggests that Mozambique's relatively high rate of population growth (2.3 percent over the period 1993-1999) needs to be brought down if medium and longer term efforts to stimulate growth and poverty reduction are to succeed.

It is also worth emphasizing that macroeconomic stability has many dimensions of a public good. When conditions are stable, confidence rises. This stimulates investment that, in turn, has spillover effects for income generation. As noted in section 5 below, macroeconomic stability also has an important effect on the poor. Economic shocks disproportionately disadvantage the very poor. Sustained periods of macroeconomic stability allow the poor some flexibility in revamping and (hopefully) beginning to move beyond their coping strategies to activities that, though more risky, have the prospect of raising their incomes and welfare.

b. Stimulate Growth in Agriculture (and Other Productive Sectors)

For most countries in Africa, and certainly in Mozambique, sustained economic growth and poverty alleviation will only occur when and if there is broad-based expansion in agriculture. The bulk of the labor force lives in rural areas with the majority of rural dwellers deriving their livelihood from agriculture and related activities. With no exceptions of any consequence, the worst dimensions of poverty in Africa are concentrated in rural areas.[46] Moreover, there are several systematic differences between rural and urban households that place the former at a disadvantage. Rural households tend to be larger than their urban counterparts.[47] The migration of adults from rural areas has raised the rural dependency ratio. This ratio has been further inflated by the practice common to urban households of sending one or more of their children to the rural areas where they are "cheaper" to raise. Losses due to HIV/AIDS have taken a greater economic toll in rural areas, with grandparents and older siblings having to assume additional burdens when parents die and families lose their principal income earners.[48] Access to education, health, and other social services is far less convenient in rural areas than in urban areas. (This pattern may be especially pronounced in Mozambique due to past security problems in rural areas.) A further difference, not widely noted, is that food security is typically higher in the urban areas than in rural areas, especially relative to rural areas that are marginal for agriculture and livestock and distant from all-weather transport routes. Finally, African governments remain highly sensitive to pressures on food supplies in urban areas. They respond quickly through official imports or the solicitation of donor support when those supplies are threatened (Bush 1996; von Braun, Teklu and Webb 2000).

The importance of rapid, sustained growth in agriculture to underpin the broader pattern of growth and poverty alleviation is one of the key lessons for Africa from the Asian experience of recent decades. The period of high rates of growth in manufacturing in Asia was preceded for a decade or more by sustained agricultural growth (Timmer 1986, 1991:147-140; Goldman 1994, 1997, 1999; AsDB 1998:104-106; Radelet and Sachs 1998; and Mellor 2000). Explaining the sharp expansion of manufacturing in Chile, Malaysia, Korea and other (so-called) "miracle countries," *The Economist* noted:[49]

> What happened in successful countries, …, is that rising productivity in agriculture, spurred by newer technology and more efficient marketing methods, allowed countries to produce more with fewer workers, releasing labour into manufacturing. The implication, however strange it seems, is that [primary] commodity exporters can best accelerate diversification and lift their growth rates by boosting the efficiency of primary-product industries.

The lesson, however, is more general. From the first industrial revolution onwards, rising productivity in agriculture and industry have been complementary (Deane 1965). Apart from city-states with special advantages of location (e.g., Singapore and Hong Kong), enduring industrial expansion has only occurred when it has been founded on sustained agricultural growth. African countries have not been, and will not be, exceptions to this general pattern. In countries such as Tanzania, Senegal, and Zambia, the stagnation of agriculture has been a major reason for generalized economic regression (McPherson and Zinnes 1991).

Promoting agriculture is not beyond the capacity of African countries. As Timmer explained (1986:47):

> The factors needed for inducing the agricultural transformation, to "get agriculture moving," involves a complex mix of appropriate new technology, flexible rural institutions, and a market orientation that offers farmers material rewards for the physical effort they expend in their fields and households and for the risks they face from both nature and markets.

The emphasis on "appropriate new technology" is noteworthy for it highlights the importance of raising productivity in agriculture. This process has to be seen as a continuous quest. To illustrate, the United States has achieved and maintained its pre-eminent position in world agriculture through rapid productivity growth. Indeed, at the time that growth specialists were attempting to explain the general productivity slow-down of the 1970s and 1980s in the developed economies, they regularly overlooked the fact that U.S. agriculture had experienced no such decline.[50] Thus, a continuing lesson for Africa (and other developing areas) from the country that has undergone some of the most profound economic transformation of any country in history is that rising agricultural productivity both fosters and sustains rapid economic growth.

While the role of agriculture in providing the basis for sustained economic growth is well established, recent research has highlighted the crucial nature of agriculture for poverty alleviation and environmental sustainability. On the latter point, Brown and Haddad (1994:2) referred to the improved management of natural resources in Kenya. They noted:

> The 'secret' of the transformation was agricultural intensification, encouraged by local land use innovations, infrastructural development, access to high-income markets, and access to off-farm income that could be reinvested in land.

Drawing together this experience and evidence from other African countries, Brown and Haddad (*ibid)* concluded:

> …addressing rural poverty in the first instance is a crucial catalyst in igniting agriculture as an engine of growth in an open economy. This requires effective programs that target assistance to the poor, raising incomes in tandem with provision of social services in the form of health care and access to safe water and adequate sanitation, thus enabling the poor to be good stewards of their natural resource base and to participate in the growth and development process.

Focusing on agriculture in Mozambique would be one of the most practical ways that the GoM could accelerate growth and begin to deal with poverty and environmental degradation in an enduring way. Agricultural specialists have long recognized that rural poverty has been directly related to low productivity (which inhibits growth). More important, they have also understood that an integrated strategy is needed to raise productivity, and thus deal with poverty (Dumont 1966; Hunter, Bunting and Bostrall 1976; Chambers 1978; Lele 1981; Johnston and Clark 1982;

Timmer, Falcon and Pearson 1983; Chhibber 1988; Sahn and Sarris 1991; IFPRI 1995; Tomich, Kilby and Johnston 1995; Binswanger and Deininger 1997; Delgado *et al.*1998).

The basic objective is to create circumstances in the rural areas where farmers have the inducement to fully exploit their comparative advantage. The policy challenge is no different now than when Adam Smith first expounded on the benefits for productivity and output of increasing the "extent of the market."[51] This idea has been particularly relevant to Mozambique where agricultural and rural activities were disrupted for so long. Due to isolation, distance, poorly developed and maintained infrastructure, the extent of the market facing rural producers has been severely limited. This has seriously constrained any net 'farm gate' returns from agricultural (and other rural-based) activities. In terms first used by T.W. Schultz,(1957:Ch.3) there has been a major contraction in the "economic supply of land" defined as the area over which, for given technology and market opportunities, the net rent from normal agricultural activities (such as the production of maize, roots and tubers, tree crops, and livestock) is positive.

Macroeconomic instability, deteriorating infrastructure, taxes on agricultural inputs and outputs (including an overvalued real exchange rate), uncertain input delivery, and sporadic harvest evacuation have combined in ways that make the risk-adjusted net returns on most agricultural activities negative. These have been compounded by problems of unreliable rainfall, the threat and stresses to crops and livestock from diseases and pests, and the food insecurity arising from the difficulties of effectively storing food in tropical settings. Thus, although Mozambique has a large and rich physical supply of land, economic and technical constraints have severely limited the economic supply of land for agriculture. By promoting agricultural growth, the GoM will reverse this trend.

c. Reform the Public Sector

A recent report of the United Nations (1999:3) describing the commitment to reduce poverty in Africa by 50 percent by the year 2015 concluded that:

> The challenges facing Africa in terms of deepening economic and social progress and sustaining it over the next two decades include addressing issues in the following critical areas: human capital, institutions, structural diversification, lowering transactions costs, raising competitiveness, good stewardship of environmental and ecological resources, and mobilizing resources for development financing.

Few development specialists will argue over the relevance of any of these measures. For Mozambique, however, the basic problem is how the necessary changes will occur. There is already a large development backlog. The human capacity to take the necessary measures is limited (and being progressively reduced due to losses from HIV/AIDS). Furthermore, the country remains overwhelmingly dependent on continued flows of foreign aid.

While the United Nations report has correctly identified the broad development problem, the most immediate challenge facing the GoM (and many other African governments) is different. That challenge is to ensure that its goals remain modest enough to be tractable. No one denies that, in general terms, the tasks of accelerating growth and alleviating poverty are urgent. But, despite the best of intentions, the GoM will fail to stimulate growth and reduce poverty if it overloads its development agenda. This is not a new problem. The African landscape is littered with failed attempts to promote growth and development, largely because governments were incapable of effectively fulfilling the responsibilities they had assumed.

As a quick way to highlight the nature of the problem, senior GoM policy makers should review all of their commitments to the IMF and World Bank over a period of (say) five years and dispassionately compare what was promised with what was achieved. For the GoM, indeed all African governments, and the IMF/World Bank (if they could be induced to take note), the exercise would be sobering.[52] Far more has been promised than has been delivered even on so-called "stroke of the pen" reforms and even in the face of the very best of intentions.

At the root of this matter is a major disconnect. This was illustrated in the Calamitsis, Basu and Ghura study cited earlier. At one point, they note:

> The successful formulation and implementation of sound economic policies in SSA [sub-Saharan Africa] is often hindered by poor management capacity, as well as by weak institutional and administrative structures (p. 17).

Though a valid observation, CBG promptly ignored it when they made their recommendations. No where do they check whether the changes they propose are consistent with the poor managerial capacity and weak structures of African governments. Like most development specialists,[53] CBG prescribe what they believe *needs* to be done to turn African countries around.

A list of what they recommend includes:

- encourage private investment,
- develop a supportive legal setting,
- ensure the government focuses on "effective" infrastructure,
- fully restore macro stability,
- sustain growth-enhancing programs,
- remove support from special groups and public enterprises,
- give central banks autonomy, and
- liberalize trade using regional integration as an entry point for full entry into the globalized economy.

Again, few specialists would disagree with the items on this agenda. At some point, all of them should be implemented. The problem, which CBG did not address, is how it can be implemented when the tasks involved are beyond the capacity of the governments involved. On this point, African governments could usefully take note of Asian experience. My colleague at Harvard University, Professor Dwight Perkins, has for many years made the case that one of the major lessons of the so-called Asian miracle is that none of the relevant governments tried to do too much at once. They did a few things appropriately–encouraged agriculture, provided some basic infrastructure, helped finance exports (*after* export orders had been obtained), maintained macroeconomic stability, and ensured that the real exchange rate was not "out of line" (Perkins 1994). Having provided a basic framework to stimulate growth, the Asian governments then added to their agenda. By contrast, governments in Africa have adopted agendas that are well beyond their capacities (technical, administrative, and financial). By doing this, their efforts have been pre-programmed to fail. It is no surprise that, in the majority of cases, they have failed. Moreover, as long as African governments continue to overload their agendas, their efforts will continue to fail.

Cutting back the development agenda so that it is in line with the government's capacity will require decisions that sort out what is essential from what is desirable. Having made that division, the focus should be on what is essential. For Mozambique, this is infrastructure (including basic security), education (especially for girls), health, and food security.

Infrastructure: Extensive statistical analysis of the impact of public investment on economic growth shows that there is little relationship between gross public investment and the rate of growth of per capita income (McKenzie *et al*. 1996; Calimitsis, Basu and Ghura 1999; and Mellor 2000).[54] One exception is the highly significant relationship between public investment in infrastructure and economic growth (World Bank 1994). This result is encouraging and fortuitous. It has been always understood that improved infrastructure is essential for growth. What is now emerging is that the expansion of physical infrastructure is also a major element in reducing rural poverty (Fan, Hazell and Thorat 1999). The result is fortuitous because expanding infrastructure, particularly roads, bridges, water supply systems, and so on, is a task that is well suited to public sector initiative.

The Education of Girls Although it has been recognized for many years that education is essential for rapid, sustained agricultural growth, what has been shown in recent research is that the education of girls is a key to growth and poverty reduction. While such emphasis already should have been compelling on welfare and equity grounds, many governments in developing countries are hesitant to formally insist that girls be given the same access to education as boys. A study entitled *The Fruits of Girls' Education* (Fritschel and Mohan 1999) concluded that:

> …educating girls offers a multitude of benefits for the girls themselves, their current and future families, and their societies. …[E]ducation helps create more productive workers and thereby improves income equity. It improves overall economic growth and leads to greater care of the environment. And it helps people adapt to the demands of globalization and to shape it.

Although the value of educating girls in now well established, what have been termed complex and persistent barriers remain. These are dimensions of gender bias. The problems of gender bias across Africa have been so pronounced that an increasing number of specialists argue that sustainable economic development is not possible without specific actions to counteract the problem. The World Bank's study *Gender Strategies for Sub-Saharan Africa: An Overview* provided guidelines that have been summarized in four strategic objectives (World Bank 1997, emphasis original; see also World Bank 1999):

One: Invest in women's *economic capacity* by improving the gender-responsiveness of **macroeconomic and sectoral policies**, increasing women's effective access to **financial services**, with a particular focus on **agriculture**, and redirecting the priorities and programs of **agricultural research and extension** to the specific needs of Africa's women farmers.

Two: Invest in women's *human development* by significantly raising female participation in **education**, and their access to appropriate **health, nutrition, and family planning** services.

Three: Reduce women's *time constraint* by expanding effective access to rural **water supply** and **fuelwood**, to transport services and technology (including for domestic transport tasks), and to appropriate **labor-saving technology** for agro-processing and domestic tasks.

Four: Support the **systematic participation** of women at all levels (macro, sectoral, micro) in identifying the gender-differentiated impacts of policies and programs, and in defining and implementing ways to overcome gender barriers in access to economic resources, and in human development.

These objectives are based on detailed time studies and household budgets from across Africa that reveal major discrepancies between the time and effort women spend working relative to men. Dealing with these deep-seated discrepancies will not be easy. Some of the difficulties involved were outlined in the "The Challenge of Inclusion," a speech delivered by the president of the World Bank to the 1997 World Bank/IMF meetings in Hong Kong (Wolfehnson 1997).

Health: With low life expectancy in Mozambique and infant mortality among the highest in the world, the expansion of basic health services (and related activities such as access to clean water) requires explicit action by the public authorities. The mutual dependence and linkages among poor health, poverty and lack of growth have been understood for many years. In 1980, the World Development Report (World Bank 1980:.35) and the Brandt Commission (1980:49) made the connection. Since then, a host of literature has added to the details (World Bank 1993; DPMN 1993; Streeten 1994; Vosti and Reardon 1997; World Bank 1997; World Bank 1998; Fan, Hazell and Thorat 1999; Gallup and Sachs 1999). Key areas of concern have been the factors linking health and nutrition, vector-borne diseases (particularly malaria), and ecological influences (especially the food insecurity induced by environmental degradation). On the last point, emphasis has lately been given to environmental health as a means of minimizing preventable health problems.[55]

A public sector activity that can have a major impact on health is the provision of safe drinking water. A common feature of poverty is the limited access to good quality water (Rosen and Vincent 1999; and Leslie 2000). Uneven and erratic supplies of water add to uncertainty and undermine agricultural productivity and food security. Furthermore, water-borne diseases detract from health. The latter highlights the need for adequate drainage of wastewater as well as improved water reticulation.

Finally, the health situation across Africa (including Mozambique) has been severely affected by the spread of HIV/AIDS. There is now a large amount of work on methods of controlling the spread of HIV. Major research has also been undertaken on the public health aspects of the epidemic and potential points of intervention. Less thoroughly researched, however, has been how to adapt training and management of personnel in the face of the large number of people who, having contracted HIV, will die prematurely.[56] Lacking wealth, these individuals are in no position to quit work. Though they may experience progressive debility, they can still make an important contribution to output and productivity, especially if they are effectively trained, compassionately managed, and appropriately motivated. Unfortunately, the principal reaction to the damage induced by HIV/AIDS has been denial and rationalization.[57] Neither of these has been a constructive way to sustain (and hopefully accelerate) growth and alleviate poverty.

A review of some of the material related to the health system in Mozambique shows that it will be exceedingly difficult to expand the scope and coverage of health related activities over the short to medium term. Problems of facilities and availability of skilled personnel seem to be the primary constraints. This is an area where what is desirable conflicts sharply with what is feasible. It is also an area where the principles of effective policy making need to be kept in focus. Policy makers should assess the current situation in the health sector relative to their stated goals of accelerating growth and alleviating poverty and then seek the next best steps to move forward. If the assessment reveals that the constraints to improving health are too severe (and too costly) to alleviate, the consequences for growth and poverty alleviation need to be understood and accepted. If, however, the expansion of key health-related activities is believed to be essential for achieving the government's medium term goals with respect to growth and poverty reduction, resources and personnel need to be reallocated from other public sector activities (official travel, infrastructure, the military, education, and so on). Again, as noted earlier, the tradeoffs are apparent and cannot be fudged. A short-term remedy for Mozambique is that it could request the donor community to add to its current assistance by devoting more resources and personnel to health-related activities.

d. Formulate and Implement an 'Aid Exit' Strategy[58]

One of the key findings of the "restarting and sustaining growth and development in Africa" study is that over the long term, foreign aid generally has a negative impact on growth. This result emerged from the cross-country comparative work and country-specific econometric models that relate aid to the growth of income. The best that can be said is that in a limited number of cases, aid has had a neutral effect on growth. No instance has arisen where aid has had a highly significant and positive impact of economic growth over the longer term. Given that African countries have received huge amounts of foreign assistance over such extended periods–for example, Liberia and Ethiopia have been assisted by the United States for more than fifty years–this is a sobering outcome.[59]

Over the period 1970 to 1998, net overseas development assistance (ODA) averaged more than 7 percent of the combined GDPs of all countries in sub-Saharan Africa (aside from South Africa and Nigeria).[60] What has this unprecedented net flow of resources accomplished? Through two editions, Cashen and Associates (1993) have insisted that foreign aid works. The message from Burnside and Dollar (1997) and others at the World Bank (1998) is less clear-cut. Aid, they state, is effective only if recipient governments maintain the appropriate (growth-oriented) policies. This has an element of blaming the victim, since none of these studies addressed whether the actions of the donor agencies enhance or undermine the effectiveness of the aid. Indeed, the World Bank study specifically avoids the question and it remains largely unresearched.[61]

Given the fact that Mozambique has received such large inflows of foreign assistance over the last two decades, it seems useful to ask whether its economic performance has differed from the majority of other African countries. If so, Mozambique would become a role model on how massive inflows of foreign assistance can promote growth and development. If not, the GoM should seriously consider how it can systematically reduce the country's reliance on foreign aid. This suggestion does not imply that aid should be eliminated, or even substantially reduced, in the short term. However, it would imply setting in place some mechanism so that senior policy makers and key public sector organizations would begin to look beyond the time when foreign assistance accounts form the bulk (or even a large) part of development funding. The goal of such an exercise would be to help the GoM and the Mozambican population avoid the situation where the large number of aid relations and activities that now exist ultimately undermine growth and development.

While Mozambique may still be at the point where such an exercise would help it avoid the worst aspects of aid dependence, other African countries (and particularly those forming part of the "restarting growth" study) are being urged to formulate and implement an 'aid exit' strategy. Again, having such a strategy in place does not mean that these countries will exit from aid soon. However, without such a strategy, there is little likelihood that they will be capable of moving beyond aid in the foreseeable future. Furthermore, if the experience of long-term aid recipients is any guide, these countries will neither grow nor develop.

Relative to GDP, Mozambique has received more aid than most countries in the world over the last decade. In view of the urgency of reconstruction and the low level of real income at which the country has been making the transition from war to peace, major aid flows during the initial years have probably been indispensable. The challenge, however, is to ensure that aid does not create conditions that erode economic performance. A lesson of history, from the time of the Marshall Plan forward, is that for aid to be effective it should satisfy three criteria (Bell 1965; Orme 1995). First, it needs to be large enough to respond to the problem at hand. Second, it should be based on the principle of self-help, implying that aid money is not used for activities to which the government does not contribute substantial amounts of its own resources. And third, the aid program should have a definite end date; i.e., a time beyond which all parties involved recognize that the aid flows will be sharply reduced (and even eliminated).

A major problem in Mozambique (and Africa more generally) is that aid flows only satisfy the first criterion, namely, they are large. There is little self-help and aid continues year-in-year-out whether or not it has been effective in promoting development (Alesina and Wedder 1999). The outcome for the last four decades (at least) is that aid to Africa has failed to help create the conditions for sustained growth and development (Brent 1990; *Economist* 1994a; UNDP 1994;

European Union 1996; and Mellor 1999). According to a recent paper produced by the Center for International Development (CID) at Harvard University (CID 1999), countries such as Mozambique will not only need major debt relief (already granted) but increased flows of aid. Missing from the CID paper, however, is any assessment of whether additional flows of aid to Africa in general or Mozambique in particular can promote growth and development. Past experience suggests that further aid will not be effective. Indeed, we should recall that CBG referred to the economic situation in Africa as fragile. Why is this the case after so much foreign aid for so long? Could it be that the large flows of aid to Africa have contributed to that fragility, rather than boosting reform and growth?[62]

There are many reasons why aid has been ineffective. Given the size of the aid it receives, one that Mozambique should take seriously is aid-induced "Dutch Disease" (Roemer 1984; Gillis *et al.* 1996,:476-480). By supplementing the supply of foreign exchange, canceling debt that cannot be serviced, and providing budget support that the domestic economy is incapable of raising in taxes, foreign aid artificially overvalues the real exchange rate. That is, it distorts the ratio of domestic to external prices in ways that undercut a country's international competitiveness. Since Mozambique continues to receive large amounts of support to finance its basic budget and balance of payments gaps, the real exchange rate continues to be overvalued by a large margin.

This is the case even though the nominal exchange rate is market-determined and stable. The underlying economic pressures associated with an overvalued real exchange rate are persistent and profound. Policy makers in Mozambique cannot assume (and moreover should not assume) that the relative stability of the nominal exchange rate implies a real exchange rate that will stimulate long-term growth. Moreover, because of the size of the aid flows, it cannot be. The policy implication is that measures need to be taken to significantly devalue the real exchange rate.

e. A Constructive Approach to Globalization

After years of seeking to cut themselves off from foreign influences as a means of promoting domestic self-sufficiency and freeing themselves from outside control, most African governments now find that this strategy has left their countries significantly poorer. Indeed, one of the ironies of Africa's experience is that countries that used the much-maligned trans-national corporations to gain access to improved technology, information, management skills, and markets have grown rapidly and developed. Countries whose leaders were effective in cutting their countries off from these influences languished. Taking their cue from Ghana's Kwame Nkrumah, African leaders such as Nyerere (Tanzania), Kaunda (Zambia), and Nimieri (Sudan) sought to minimize the influence of the multinationals. Their strategies worked only too well. Many of the best enterprises pulled out. The outcome was an extended period of low foreign investment with technology in Africa falling further out of line with world trends. The whole episode was a practical demonstration Joan Robinson's dictum: the only thing worse than being exploited by a capitalist is not being exploited at all.

An increasing number of African leaders are recognizing that their countries have been marginalized in world trade and exchange (Collier 1995; World Bank 1995; Yeats *et al.* 1997; Rodrik 1998; Collier and Gunning 1999). Many of these same leaders now devote considerable effort to attending international forums and conventions trying to convince foreign investors of the economic opportunities available in their countries (Cockcroft 1992; GCA 1996; UNCTAD 1996; USDC 1997; Bennell 1997; Bhattacharya, Montiel and Sharma 1997; ADB 1997; Clow 1997; Goldberg 1997; Gastanaga, Nugent, and Pashamova 1998; Sachs and Sievers 1998; Harris 1999; Government of Kenya 1999). These efforts, however, are being hampered by some counterproductive approaches to economic management. Two are discussed here: the problem of budgeting in the context of global influences, and macroeconomic stabilization in the face of financial flows.

Budgeting in the Context of Global Influences: Most budgeting exercises across Africa begin with estimates of current-year spending.[63] These are then increased in line with some broad measure of inflation and the expected growth in real income. The implication is that the ratio of government expenditure to GDP will remain roughly constant. Preliminary projections of revenue are then derived. Often these are estimates of current year collections inflated by a number close to the expected growth of nominal GDP. The further implication is that the ratio of revenue to GDP will remain constant. From these data, an estimate of the deficit that needs to be financed is derived. Preliminary projections of net borrowing from the non-bank public (typically small), net non-concessional foreign borrowing (often zero), and foreign aid yield an estimate of the financing gap that has to be covered by extraordinary measures. Such measures include bilateral debt relief from the Paris Club, “fifth dimension” funding from selected donors, and special assistance arranged through the Consultative Group (CG) mechanism. Based on the expectation that the donors will cover the gap, especially if the country has an IMF program, African governments introduce their budgets and press on with their expenditure plans.

Now so common in Africa, the above procedure has become institutionalized. The net result is that most African countries cannot effectively finance their budgets until after their expenditure plans have been presented to the donors who assemble at CG meetings or the Paris Club. With few exceptions, such meetings take place *after* the financial year is underway. But due to delays in the arrival of donor support or systematic understatements of the government’s actual expenditure plans, there tends to be a shortfall in financing. The shortfall is then typically covered by domestic bank finance. The outcome is that most budgeting exercises across Africa have an inflationary bias.

Though the above approach to budgeting is by far the most common in Africa, it is inconsistent with effective management of the macro economy. It is especially counterproductive under conditions created by financial globalization.[64] Those conditions invariably foster asymmetric pressures in the sense that financial resources flow out of African countries much more readily than they flow in.[65] To take account of this asymmetry, the budgeting exercise should be conducted in reverse order. Expenditure plans should be prepared only after realistic (i.e., conservative) estimates of the (non-inflationary) resource envelope, both foreign and domestic, have been determined. A major benefit of this approach is that it would eliminate all recourse to “extraordinary finance” which, despite, its title, has become institutionalized as a means of funding African governments. This would encourage African governments to plan well in advance of their budgets. It would also help cut through the various ‘games’ with and against the donors as African countries gain access to the “extraordinary finance.” Under current arrangements, it is too easy for African governments to deflect attention from their non-performance by blaming donors for not providing aid at the time or in the amounts deemed necessary. Deriving the budget in this way offers a "safe-fail" approach to managing public expenditure. That is, expenditure commitments are made only after firm revenue sources have been secured, not the other way round.

Macroeconomic Stabilization and Financial Flows: With few exceptions the financial turmoil in Asia during 1997 and 1998 did not directly spill over to Africa. Some African leaders and senior policy makers even noted that the lack of financial disruption experienced by their economies vindicated their resistance to IMF/World Bank and other donors who had been pressuring them to "open up." This argument misses the point.

Notwithstanding the immediate financial difficulties, it is important to see Asia's financial difficulties against the preceding three decades of rapid growth and development. It is also worth noting the resilience of the most seriously affected countries (Korea, Thailand, Philippines, and Indonesia). Most have bounced back, some in dramatic fashion. Korea's real income declined by 7 percent in 1998. In 1999, it grew by 10 percent. Recent projections for 2000 suggest that real growth will be 8 percent.

Most African countries were spared the financial turmoil only to be adversely affected by the subsequent decline in commodity prices. (Copper and gold are two of several key African exports whose prices declined sharply.) However, they have not proved to be so robust. The turnaround in Africa is taking (and will take) considerably longer.

This raises a second point. In global financial terms, African countries do not need to "open up." They are already open. Foreign investors and local asset-holders have had ample time and many opportunities to assess the viability of potential investments. The overwhelming outcome (which still applies) has been that the majority of investors (local and foreign) have "voted with their feet." Considered in general terms, African countries have not offered investment opportunities that, on a risk-adjusted basis, can compete with those available elsewhere.[66] The evidence, now widely available, shows that African countries have undergone large-scale capital flight as local asset-holders shifted their resources to safe havens. Furthermore, African countries have received minimal amounts of foreign investment (around U.S. $1 billion per year on a net basis). The only important investments in African countries have been confined to areas and activities where strategic concerns outweigh idiosyncratic risks. The development of Equatorial Guinea's oil reserves is an example.

To better understand the nature of the risks, one need only ask why Sani Abacha, Mobutu Sese Seko of Zaire, The Gambia's Dawda Jawara, Robert Mugabe of Zimbabwe, Kenya's Daniel Arap Moi and a host of other past and present leaders have been unwilling to invest their own resources in Africa. More than anyone else, they appreciated the risks involved and sought safer outlets abroad.

The implication for senior policy makers in Mozambique is that globalization has already fundamentally influenced the growth potential of the country. Private investment can only be increased through policies that induce local asset-holders to keep their resources on-shore and allocate them productively. Foreign investors will typically only participate when they perceive that local individuals and enterprises are willing to invest as well. Public investment can (at best) complement private investment; it cannot substitute for it. The challenge for the GoM is to create a setting in which the potential risk-adjusted returns on private investment are commensurate with those available abroad. For that to occur, policy makers need to appreciate the problems created for investors by irreversibility and the damage that can be done to investor confidence when the government capriciously reverses policy direction or allows the macro economy to become unstable.

Globalization offers opportunities for, and imposes constraints upon, every economy. Writing in *The Lexus and the Olive Tree,* Tom Friedman (1999) correctly argued that globalization has not failed African countries. With few exceptions, African governments have failed to develop the policy setting, institutional base, and governance structures that would allow their citizens to respond constructively to globalization. A useful exercise for the GoM would be to assess how its policies measure up in this regard.

5. Special Considerations Relevant to Mozambique

The strategy derived by the researchers who have studied the issues related to "restarting and sustaining growth and development in Africa" provides broad policy directions. Each country, however, has special considerations. For example, the direct concerns that confront Uganda because it is land-locked are not directly relevant to Mozambique or Tanzania. These two will be deeply concerned about the use of the resources on the continental shelf. Furthermore, given Mozambique's location at the tail-end of a river system serving seven countries (eight including South Africa), the issues of river basin management and the international distribution of available water supplies will be important. Finally, while African countries that are close to Europe can focus on mass tourism, Mozambique's location requires it to emphasize up-scale tourism.[67]

This section closes the essay with a discussion of several issues that may need to be considered in developing a strategy for accelerating growth and alleviating poverty. The issues relate to the emphasis that should be given to trade as a means of promoting growth, building upon the coping strategies that large groups of the population already have in place, understanding and enhancing the micro level impact of key macroeconomic changes, and regional cooperation. We conclude with an assessment of whether policies can be designed to allow Mozambique (as one analysts put it) to "have it all"–rapid growth and poverty alleviation without further damage to the physical environment.

Trade as a Means of Promoting Growth? The data provided earlier in Table 1 and *Mozambique at a glance* highlight a major structural imbalance in trade flows in Mozambique. Over the period 1990 to 1997, exports of goods and services as a share of GDP averaged 18 percent while imports of goods and services averaged 47 percent of GDP. (More recent data shows that the trends worsens markedly after 1997.) The table also shows that over the same period, Mozambique's external debt was the equivalent of more than 250 percent of GDP. Responding to the damage created by recent floods and Mozambique's record of economic performance, the international community has already provided large amounts of debt relief.[68]

The debt relief has been a major positive step. Nonetheless, policy makers and GoM officials should recognize that, as the economy is currently structured, the relief is at best temporary. *If* large imbalances in the structure of trade persist, Mozambique can never be out of debt. The trade imbalance represents a persistent increase in the use of Mozambique's international savings. Until now, donors have provided the necessary capital to alleviate the savings draw-down through grants. However, these funds may not be available in the future. The foreign debt situation in Mozambique can only be resolved by moving the trade accounts back into balance.

A major question is how the government can do this. A combination of measures will be needed. As explained earlier, one such measure will be a major real devaluation of the exchange rate. This is needed as a means of stimulating exports and discouraging imports, as well as to achieve a sharp reduction in unit labor costs.[69] As unit costs decline, explicit policies to promote exports will be needed. There is controversy over how this should be done. Conventional approaches to economic development see rapid export growth as being essential to raising the overall rate of economic growth (Dornbusch and Helmers 1988; Laird and Nogues 1989; de Rosa 1991; Dollar 1992; Lindauer and Roemer 1994; Yeats *et al.* 1997; Sharer 1999). This has been supported by a large number of estimates derived from Barro and Sachs/Warner-type single equation growth studies which invariably find a highly positive statistical relationship between the growth of real income and exports (or trade defined as exports plus imports). (The study by Calamitsis, Basu and Ghura cited earlier is a more recent example.) Accordingly, many strategies have been devised to promote exports. "Export-led" or "outward-oriented" growth has been widely seen as means of moving African countries forward (Gillis *et al.* 1996:523-524; Madavo and Sarbib 1997; Fischer, Hernandez-Cata and Khan 1998; OECD 1998; World Bank 2000a:Ch. 7)

Some prominent trade specialists have raised questions about this relationship (McCallum 1995; Rodrik 1997; Summers 1999; Frenkel and Romer 1999). Recent research has moved beyond single equation approaches to models that specifically allow for the mutual interactions among income growth, trade and other macroeconomic variables. When this is done using African data, the strong direct association between trade and growth, evident in single equation approaches, disappears (McPherson and Rakovski 2000).[70] A far more complex pattern of direct and indirect inter-dependence emerges.

This research shows that when the growth of income is regressed on trade in the context of a simultaneous equations model, the coefficient is positive but not statistically significant. When trade is regressed on the growth of income in the same model, the coefficient is positive and highly statistically significant. There is, however, a strong indirect association between income growth and trade via the real exchange rate. The nominal exchange rate is dependent upon trade. The inflation rate depends positively on the exchange rate. And, the growth of real income depends on the real exchange rate (thereby combining the effects of the nominal exchange rate, external prices and domestic prices).

Teasing out the relationship in this way does not mean that trade is unimportant for growth. However, these results challenge what has almost become a truism in the development literature– that trade is an engine of growth. At the risk of overstating the point, the evidence suggests that in Africa's case, growth has been an engine of trade. Indeed, this is consistent with the observation by Rodrik that, when measured relative to GDP, African countries trade no less on average than countries in other regions (Rodrik 1998). When seen this way, Africa's marginalization in world trade and exchange over the last three decades has resulted from a lack of growth rather than a lack of trade.

For policy purposes, the above results underscore the complementary relationship between trade and growth. Economic policies need to be designed to take advantage of the direct and indirect links between trade and growth. Such policies will include promotion of macroeconomic stability, maintenance of an appropriate real exchange rate, investment in infrastructure, and support for improvements in health and education. These will rebuild confidence, raise the rate of investment, and improve productivity. None of these recommendations is surprising. All countries that have grown and developed on a sustained basis have taken steps to build upon the linkages between domestic and trade-based activities.

Build Upon Coping Strategies: As discussed in section 3, a dominant feature of poverty is insecurity. When faced with extreme insecurity the poor adopt various coping activities. Given Mozambique's recent economic performance and record of recovery, it may not be obvious how the issue is relevant to the task of accelerating growth.

Coping strategies are relevant precisely because they are so conservative. The poor will not abandon or radically modify them readily. Thus, although conditions have been improving in Mozambique, it will take some time and a clear demonstration that conditions have changed permanently for the poor to begin taking the risks needed for them to fully benefit from the economic recovery. There are some in Mozambique, impressed with changes made so far, who feel confident enough to begin investing or engaging in higher productivity (and hence more risky) activities. Many others, however, will wait. They will want to see evidence that the changes in Mozambique are being sustained. Even then, most of the very poor will only unravel their coping strategies gradually.

In this respect, policy makers face a two-fold challenge. They need to maintain the momentum in the economy so that an increasing number Mozambicans can begin to move beyond activities that enabled them to avoid destitution. Policy makers also need to avoid shocks in order to reinforce the general build-up of confidence that conditions have changed for the better in an enduring way. Since shocks always arise (the most recent examples being floods and oil price increases), policy makers need to ensure that the economy builds up some safety margins in key areas. At the macro level, these safety margins include a cyclically balanced budget, adequate foreign exchange reserves, a positive real interest rate policy to strengthen the local financial system, and movement (as rapid as practical) to a sustainable current account deficit on the balance of payments.[71]

Micro Effects of Macro Changes: The promotion of economic reform throughout Africa has been based on the presumption that once restrictions and distortions are removed from the economy, the induced supply response will provide a foundation for sustained growth and development.[72] International experience, particularly outside Africa, has shown that economies will respond systematically if economic reforms are implemented *and* sustained. The African experience has been mixed at best. Some analysts have argued that economies have to stabilize before they can promote structural adjustment (Roemer and Radelet 1991). This view is contradicted by developments in Russia where the economy has been edging toward macroeconomic stability through a massive program of structural adjustment and privatization (*Financial Times* 1997; Nesterenko 2000). Other analysts have insisted that structural reforms have to be undertaken in a particular sequence. Indeed, there is now an extensive literature suggesting appropriate and even optimal ways to sequence policy reforms (McKinnon 1982, 1991; Edwards 1984, 1986, 1992; Bruno 1985, 1995).[73] In practice, however, successful reforms have been phased in numerous ways, none of which was optimal *a priori*.[74]

When seen from a broader perspective, these recommendations are fundamentally concerned with the micro effects of macroeconomic reform. Some research has been devoted to how macro effects filter through the economic system to the micro level, but the basic transmission mechanisms remain unclear.[75] The (so-called) supply response reflects the change in economic behavior of selected individuals and groups as they take advantage of the changes in constraints and opportunities induced by economic reform. The relative strength and speed of these behavioral changes depend on the degree of confidence by individuals that the reforms will be sustained. Since most African governments have such a long history of start-stop reform, it is not surprising that the supply response in most countries has been weak.[76] This is *not* a reflection of the private sector's unwillingness to respond, as many government officials try to argue. When freed from the probability of arbitrary government intervention, African entrepreneurs respond vigorously. The dynamism of the informal sector is direct evidence. The lack of formal sector response can be directly linked to the signals provided by public policy. Many of those signals are confused and contradictory.

The 'banal' point made by Srinivasan in his critique of the draft 2000/01 *World Development Report* is worth repeating–no one voluntarily chooses to be poor.[77] They are poor largely because there are constraints (including misfortune) that systematically erode their income and wealth or hinder their attempts to earn income and accumulate wealth. Start-stop reform that undermines confidence is one such constraint.

The basic problem is *not* that macroeconomic reform does not (or cannot) induce a supply response. The problem has been in sustaining the reforms long enough to convince the micro level operators that the various coping strategies and other defensive mechanisms they have been using to insulate them from economic instability can be dismantled. Most governments have been slow to understand that a major problem in generating a supply response has been their own policy reversals, conflicting policy signals, and indifferent policy implementation.

For the GoM, the basic lesson is predictability and consistency based on the adoption of a feasible development agenda. Confidence needs to be rebuilt. This will be a slow process. It cannot be rushed. It can, however, be readily and rapidly undone by erratic government behavior based on a start-stop approach to policy implementation.

Regional Concerns: There has been a huge amount of effort devoted to regional issues in Africa. Radelet (1997) noted that there are more than two hundred organizations whose mandate includes the promotion of regional trade and cooperation. Numerous groups designed to foster closer association among neighboring countries have been formed. Looking further to the future, African countries have a commitment, contained in the Abuja Declaration of 1991, to move the whole of Sub-Saharan Africa to a common market by the year 2020.

Though the plans have been bold and the intentions admirable, action so far has been timid and halting. Even when allowance is made for parallel market activity, intra-Africa trade and financial flows remain extremely modest.[78] A major problem has been that most African countries cannot agree to trade on a bilateral basis, let alone agree in ways that would make multilateral relationships effective (Hawkins 1993; AERC 1997; Oyejide, Elbadawi and Collier 1997; Gibb 1998).

This should not be unexpected. It reflects the deeply held reservations by African leaders regarding the question of economic liberalization. Regional trade and cooperation has often been seen as the thin end of the wedge to more comprehensive economic, social, and political liberalization. Development specialists, however, have sought to use regional trade and cooperation as a transition phase to help highly distorted countries prepare for more penetrating involvement in the international economy. Growing concern over Africa's marginalization in the world economy, however, has made the issue of regional integration increasingly attractive. For African leaders, the attraction is that it allows their countries to overcome the disadvantages of small markets, remoteness, and a limited production base without fully embracing the rigors of free trade.

A major problem is that, under present circumstances, most regional trade groups in Africa offer few advantages. Many of them overlap in confusing and disruptive ways. They also divert scarce resources (skills, effort, and finance) to largely fruitless efforts associated with making marginal additions to small markets. Additionally, they divert attention from the larger challenge of ensuring that African countries become fully integrated into world trade and commerce.

Nevertheless, some regional efforts have been effective. For example, with African countries re-emphasizing the importance of infrastructure in growth and development, a framework for multi-national cooperation has been emerging. Examples where such cooperation has occurred is in transport corridors, the upgrading of road and rail networks, and the rationalization of power generation and distribution.[79] Such efforts provide a foundation for future regional cooperation.

The power grid in Southern Africa is obviously a key concern for Mozambique. This, however, raises the issue of access to water resources. Abstracting from the devastating floods this year, Mozambique has been adversely affected by recurrent drought throughout Southern Africa.[80] Low rainfall and limited run-off in the Zambezi River basin over the last two decades have seriously affected water levels in the Cabora Bassa dam. This has important implications for the generation of electricity, and causes saltwater intrusion and (hence) ecological damage in the Zambezi River delta.[81] Since Mozambique is at the tail end of the Zambezi River, it stands to lose substantially if management of the basin is not coordinated. This is a policy issue that time will exacerbate rather than ameliorate. It is clearly an issue in which Mozambique could begin exercising leadership before too many options are foreclosed, as countries further up the basin begin drawing more heavily on the available supply.

Having It All: Building upon years of accumulated research that underscores the indispensable role of agricultural progress in promoting growth and reducing poverty, Peter Hazell (1999) has argued provocatively that African countries can "have it all"–agricultural growth, poverty alleviation, and environmental sustainability. To do this, policy makers need to take advantage of the complementary relationships between the different levels of social, economic, and biological systems.

Hazell's approach has been designed to achieve broad-based development of agriculture by focusing on expanding the output of small and medium-sized farms. Such a strategy would be market-driven and supported by decentralized services that encouraged participation, particularly on the part of women. Agricultural research would focus on technological changes that do not degrade the resource base.[82] According to Hazell (1999:1):

> Such growth can reduce food prices while increasing farm incomes; is employment intensive; and increases the effective demand for nonfood goods and services; particularly in small towns and market centers. By reducing poverty and promoting diversification in rural areas, it also relieves livelihood demands on the natural resources base.

Promoting agricultural growth requires innovation, infrastructure, inputs, institutions, and incentives as well as attention to what Hazell called equity and environmental "modifiers." The "equity modifiers" include:

- Broad-based agricultural development,
- Land reform,
- Investment in human capital,
- Activities ensuring that agricultural services reach women,
- Participation of all stakeholders in setting development priorities, and
- Active encouragement of the rural non-farm economy.

The "environmental modifiers" for sustainable agricultural development are:

- Giving a high priority to backward regions;
- Focusing agricultural research on issues related to sustainability;
- Providing farmers with secure property rights;
- Privatizing common property resources where possible to ensure appropriate management;
- Modifying through taxes and charges the incentives facing polluters and degraders;
- Improving performance of relevant resource-related public institutions;

- Correcting the price distortions that encourage environmental degradation (Gillis *et al*:167-177); and
- Establishing monitoring systems to track changes in conditions of key resources.

Several of these “modifiers” are components of longer-term strategies for promoting growth and development that I have already covered. What is important in Hazell’s approach from a growth and poverty alleviation perspective is the emphasis given to participation of stakeholders, concern for issues that confront women, efforts to secure property rights, the provision of appropriate incentives, and efforts to promote the sustainable resource use.

For reasons of ‘capacity overload’ noted earlier, these activities will have to be implemented selectively over time. Nonetheless, the combination of activities highlights for policy makers the importance of building upon initiatives that have the rapid growth of agriculture as their starting point.

6. Concluding Comments

The GoM has been seeking ways of promoting rapid economic growth and poverty reduction. This paper has drawn on a range of international experiences to help identify some of the key issues that will need attention if these goals are to be met in a sustained way. There are seven points.

- Poverty reduction will not occur in Mozambique unless there is rapid economic growth. Government policies should focus on promoting and sustaining rapid growth.
- Rapid economic growth cannot occur in Mozambique without broad-based expansion in agriculture. Efforts to promote industrialization independently of a rapidly expanding agricultural base have not been and cannot be sustainable. Nor can such efforts succeed in reducing poverty.
- The indispensable foundation for rapid economic growth is macroeconomic stability. This requires attention to monetary and fiscal policies, exchange rate management, and debt management. There has been progress over recent years in stabilizing the economy. Furthermore, the recent debt relief operation has substantially reduced the risk of further debt shocks. Nonetheless, policy makers will need to ensure that the large inflows of foreign assistance do not continue to artificially overvalue the real exchange rate. Enough problems still confront Mozambique, without allowing foreign aid to create “Dutch disease.”
- The GoM should drastically reduce its development agenda in line with its capacity to implement *and* sustain policy reform. Starting out modestly and building upon a solid foundation of achievement will be far more conducive to economic growth and poverty reduction than tackling an agenda that is beyond the government’s capacity.
- As a means of focusing the attention of all Mozambicans on the task of promoting sustainable development, the GoM should formulate and begin implementing an ‘aid exit’ strategy. Though the flows of aid are unlikely to diminish over the medium term whatever the government does (short of abandoning reform), such a strategy is

required now so that aid dependence (already extreme) does not block growth and poverty reduction.

- The government needs to be sensitive to the problems of insecurity and lack of confidence that remain in the wake of the country's long history of disruption and disorganization. The conservative patterns of behavior among individuals will give way to more enterprising approaches over time. But this will only happen if there is a permanent basis by which confidence is re-established and maintained.
- Finally, GoM officials need to fully grasp and respond to the implications of globalization for Mozambique's future growth and development. The challenges and opportunities need to be understood. Two areas of particular importance are budgeting and financial management.

International experience now shows that there are many fruitful approaches available to promote growth and reduce poverty. For a country like Mozambique, with low income, a long history of economic disruption, limited physical and human capacity, and acute aid dependence, the potential strategies are limited. Rapid economic growth founded upon the broad-based expansion of agriculture is essential. So too are government initiatives to improve health, education, and basic infrastructure.

Yet, success in promoting growth and reducing poverty can only come if the government remains modest in what it attempts. The danger of over-reaching is high. The potential agenda is so demanding. The obvious needs are so pressing. Nonetheless, the GoM has to resist the temptation to over-stretch its development agenda. In this regard, the dictum of the new Managing Director of the IMF is highly appropriate. He argues that in the area of economic reform "less is more." This is advice that GoM policy makers and officials could productively heed.

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Endnotes

[1] The International Monetary Fund has produced a series of excellent reports on Mozambique. Notable among these is IMF (1998) which deals with key macroeconomic issues–money and inflation, growth and investment, wage dynamics, external competitiveness, and social sector spending. Of direct relevance to the current report is the study on growth and investment. Among other things, it shows that although the supply of investible resources in Mozambique is large (largely aid flows), the productivity of investment is low.

[2] HIPC is the highly indebted poor country debt initiative, launched with much fanfare by the World Bank and major industrial countries in 1996. Modified a number of times to help fulfill its original billing as a debt exit strategy, HIPC has provided little benefit to any of the highly indebted poor countries. Mozambique is one of the few exceptions.

[3] This research has been supported under the USAID-funded Equity and Growth through Economic Research (EAGER) Project. Several volumes are currently being prepared. McPherson (2000) presents the overall framework and several studies on the key theme in that framework.

[4] The World Development Report 1999/2000 (World Bank 2000, pp.275-6 and Table 4) describes the various poverty measures and the adjustments used to obtain comparability over countries. Measurement problems are formidable (World Bank 1990, Ch. 2). Data for developed countries have many of the same problems (biases, distortions, exclusions) making poverty measures difficult to compare over time (Atkinson 1998; Mangum, Sum and Fog 2000).

[5] A selection of literature on these topics includes: OAU 1979, 1980; Mazrui 1980; Bates 1981; World Bank 1981, 1984, 1986, 1989, 1990, 1991, 1994, 1995; Lele 1981, 1989; ODI 1982, 1992; Roemer 1982; Hyden 1983, 1990; Moors 1984; Brown and Wolf 1985; McNamara 1985; Sandbrook 1986, 1987, 1993, 1996; United Nations 1986, 1996, 1999; Obasanjo 1987; Harrison 1987; Iliffe 1987; Lamb 1987; Mabogunje 1989; Lopez and Thomas 1988; Parfitt and Riley 1989; Abernathy 1989; Nyang'oro 1989; Commins 1989; ECA/OAU 1989; World Bank/UNDP 1989; Ward 1989; Serageldin 1989; Callaghy 1990; Herbst 1990; Ravenhill 1990; Klitgaard 1990; WINROCK 1991,1993; Frimpong-Ansah 1991; McPherson and Zinnes 1991; Svedberg 1991; Collier 1991; von Braun 1991; Gallagher 1991; Thomas *et al.* 1991; Rimmer 1991; Ayittey 1992, 1998; Eicher and Baker 1992; Lavy 1992; Hyden and Bratton 1992; Ghura and Grennes 1993; USAID 1993; Easterly and Schmidt-Hebbell 1993; van Drunen and van der Kraaij 1994; Schatz 1994; Cornia and Helleiner 1994; Lindauer and Roemer 1994; Larsson 1994; van de Walle 1994; Widner 1994; *Economist* 1994; Rouis, Razzak and Mollinedo 1994; Bouton, Jones and Kiguel 1994; Sahn 1994; McPherson and Radelet 1995; CDR 1995; Collier 1995; Berthelmy 1995; Easterly and Levine 1995; Ghura and Hadjimichael 1996; Stern and Gugerty 1996; Husain 1996; GCA 1996; Lensink 1996; Schmidt-Hebbel 1996; USTR 1996; Odedokun 1996; Ndulo and van de Walle 1996; IRIS 1996; Gyimah-Boadu and van de Walle 1996; Sahn, Dorosh and Younger 1996; Sachs 1996; Demery and Squire 1996; Thomas 1996; Bush 1997; Bennell 1997; Madavo and Sarbib 1997; Yeats *et al.* 1996, 1997; Oyejide, Elbadawi and Collier 1997; Stryker 1997; Sachs and Warner 1997; IMF 1997; HIID 1997; Goldberg 1997; Block 1998; Bloom and Sachs 1998; Mellor 1998; Fischer, Hernandez-Cata and Khan 1998; McPherson and Goldsmith 1998; Bensen and Clay 1998; Rodrik 1997, 1998; Gray and McPherson 1999; Collier and Gunning 1999; Dollar and Easterly 1999; Goldsmith 1999; Ndulo and O'Connell 1999; Duesenberry, Goldsmith and McPherson 1999; Freeman and Lindauer 1999; Calamitsis, Basu and Ghura 1999; Sharer 1999; Amaoka 2000

[6] Consultation Draft January 2000 [available at www.worldbank.org/poverty/wdrpoverty]

[7] In a widely circulated memo entitled "Critique of the draft WDR Attacking Poverty," Srinivasan (2000) criticized the authors for failing to provide any vision for dealing with poverty. He was especially critical of the *dirigiste* approach being proposed.

[8] Personal correspondence with Steven Radelet (June 2000), currently with the United States Treasury.

[9] Well known studies include Kuznets (1966), Chenery and Syrquin (1975) and Syrquin and Chenery (1989). Kuznets described the systematic changes (urbanization, industrialization, and the demographic transition) that accompany modern economic growth. Chenery and Syrquin provided detailed statistical analyses of what they called "patterns of growth" that were associated with systematic changes in demand, supply, trade, and "social processes." A quick overview of changing approaches to economic growth over the last four decades can be readily traced in the six editions of Meier's *Leading Issues in Economic Development* published over the period 1965 to 1995.

[10] Friedrich Engels' *The Condition of the Working Class in England*, first published in 1845, is well known. The writings of Charles Dickens highlight many of the excesses and inequalities of industrial England. The arguments of Karl Marx were based on the view that the persistent extremes of poverty would lead to the eventual collapse of the capitalist system. Finally, Disraeli's characterization in *Sybil* of the two cultures created by industrialization in Europe is an image that has survived to the present day.

[11] Sachs (1997) has a useful survey of the major issues.

[12] The American Academy of Arts and Sciences sponsored a conference with this title in the early 1970s (*Daedelus* vol.102, no.4, Fall 1973). Brooks (1973) was convinced, and particularly convincing, that a "no-growth' strategy was a dead-end. He noted that technological advance would have to continue simply to enable the world's systems to adapt to the changing availability of resources.

[13] The USAID Assistant Administrator for Africa Vivian Lowery Derryck (1999) recently defined "sustainable development" as "…broad-based economic growth which aims to protect the environment, enhance human capabilities, uphold democratic values and improve the quality of life of the current generation while preserving the opportunities for future generations."

[14] Based on data from the World Bank (*World Development Indicators*), the per capita income of Zambia in 1965 was US $294. Korea's per capita income at that time was US $ 106. Corresponding data for GDP were $1.1 billion for Zambia and $3 billion for Korea.

[15] The data refer to 1993.

[16] The relative performances of the two economies were not differentiated by the *fact* of corruption. Both countries have been well known for high-level corruption over extended periods. The difference has been in the consequences of corruption. In Korea, there have been limits to the amounts mis-appropriated and, in large part, the resources have been reinvested in Korea. In Zambia, there have been few limits and the resources were invariably moved abroad. There are now many references to corruption and the problems it creates (Dumont and Mottin 1980; Klitgaard 1988, 1990; Frimpong-Ansah 1991; Ayittey 1992, 1998; Harsch 1993; Bush 1996; IRIS 1996; Goldberg 1997; Bardhan 1997; Kaufmann 1997; Gray and Kaufmann 1998).

[17] According to Krugman (1990), historical evidence shows that long-term (i.e., a century or more) improvements in economic welfare can be almost entirely attributed to improved labor productivity.

[18] Killick and White (1999, p.3) noted that the "record of state failure is such that its potential to deal with [poverty] problems is limited." A similar argument appears in Rahnema (1997). Governments often create the conditions that generate poverty (Stiglitz and Squire 1998). Yet, governments can also take the necessary actions to relieve poverty. This ambivalent conclusion was evident in Shipton's (1990) review of famines in Africa. He found that while governments often aggravated food shortages, remedies also required government action. In the same vein, Mellor (2000) argued that agricultural development was not possible in poor countries without specific (but constructive) government intervention.

[19] Two examples are instructive. China achieved a radical redistribution of assets at the point of a gun in the early 1950s. It was not until the late 1970s that rapid growth became the norm. Yet, for that to materialize, the Chinese

government had to fundamentally change the structure of micro incentives (through the 'responsibility system'). A second example is Zimbabwe where President Mugabe and his associates believe that extra-legal means of land redistribution (i.e., squatting) will reduce poverty. That may not be the case. If investment and income collapse, overall poverty in Zimbabwe is likely to increase.

[20] That task has been exceedingly difficult even in the developed countries. Despite rapid growth and low unemployment in the United States over the last two decades, the distribution of income and wealth has become increasingly skewed. A similar pattern has emerged in Western Europe, even though the governments there are committed the redistribution of income and wealth. A major recent concern, particularly in the United States, has been the inter-generational transfer of inequality through lack of access to health, education, and employment (FRBNY 1999). On an international scale, an explanation of inequality has been the systematic devaluation of unskilled labor due to the rapid expansion of the knowledge-based economy (Mead 1990; World Bank 1995; FRBNY 1995). This point is reinforced by recent studies of poverty and inequality in Latin America and the Caribbean (Lustig and Arias 2000). Their analysis shows that macroeconomic instability aggravates inequality. During a slump, the poor lose ground. These losses are rarely recovered during any subsequent boom.

[21] Ibi Ajayi 1997 has some estimates for African countries.

[22] Johnson (1973) illustrated how capital mobility constrains domestic policy. More recently, Humpage and Osterberg (2000) highlighted how United States policy is constrained by capital mobility.

[23] The literature is vast. Useful surveys are contained in Okhawa (1993), Nelson (1996), and Jorgenson (1996) and Nell (1998).

[24] A similar point is made in Collier and Gunning (1999a) and World Bank (2000a) in their study of why African countries do not grow. Their argument is that because transaction costs are systematically higher in Africa, the scope for mutually rewarding trade is limited. With a lower surplus, investment and growth are lower.

[25] Corden 1966; Johnson 1967; Bruno 1972; IMF 1987; Khan and Lizondo 1987; Killick 1987, 1993; Balassa 1988; Edwards 1989; Reisen 1989; Pinto 1990; Dornbusch 1990; de Rosa 1991; Devarajan and de Melo 1991; Thomas, Nash *et al.* 1991; Frimpong-Ansah, Kanbur and Svedberg 1991; Fischer 1993; Nash 1993; Krueger 1993, 1997; Edwards 1993; Hill 1994; Rodrik 1995; Clement 1995; Duesenberry *et al.* 1996; Goldsbrough *et al.* 1996; Agenor and Montiel 1996, Ch.6; Engel 1996; Asea and Reinhart 1996; Stryker 1997; Paus and Robinson 1997; Knight 1998; Ancharaz 1998; Lall 1999

[26] Solow (1997) expands on the idea of "learning by 'learning-by-doing'" while Pissarides (1997) emphasizes the importance for developing countries of "learning by trading."

[27] This was reported on 13th September, 2000 in the BBC series Africa Report (www.bbc.co.uk) under the heading "Nigeria tops corruption chart." Transparency International's findings are not "one-off" for Mozambique. A pattern of persistent corruption has been confirmed by several rounds of the *Africa Competitiveness Report* supported by the World Economic Forum. GoM policy makers have a course for action. The first is to take measures that sharply reduce corruption and then convince outside investors that those measures will remain effective. The second is to repair Mozambique's image by the continued implementation of prudent policies in an open, transparent way. Something has to be done at the senior most levels of government down. The current setting will not generate the type of long term investment needed to raise growth and reduce poverty on a sustainable basis.

[28] Moreover, both mistakes are relatively common. A recent review by Gupta *et al.* (2000, pp.95-102) reports the work of several studies showing that many of the benefits from government efforts to address poverty flow to those in upper income groups.

[29] This is a key idea behind the increased recent interest in "global public goods" (HIID 1997; Kaul, Grunberg, and Stern 1999). The argument is that some benefits (improved health and vigorous economic growth) are so compelling in terms of aggregate welfare that the international community has an obligation to ensure they are realized.

[30] World Bank and International Finance Corporation "Country Information Center" web site "Mauritius Country at a Glance" [available at www.worldbank…N/cic/mauritius]

[31] Although the income share fell, the real incomes of the lowest 20 percent rose sharply during the 1980s. Moreover, the income share of the lowest 20 percent was high relative to other African countries (*African Development Indicators 1988/99* 1998, Table 13.3).

[32] There has been no mystery why developing countries in general have experienced what has been referred to as a "food problem" (large amounts of resources in agriculture but with productivity so low they cannot generate a food surplus adequate to support the entire population) and developed countries generally have had a "farm problem" (few resources in agriculture but because of their high productivity too many to sustain the incomes of farmers without generating large agricultural surpluses). Developing countries, in general, have taxed their farming communities both directly and indirectly. Developed countries, in general, have done the opposite. The Uruguay Round and the activities of the "Cairns Group" have made some progress in dealing with this issue (World Bank 1996). For a specific developing country, the lesson is clear: remove all impediments, direct and indirect, to agricultural production and rural activities. For Mozambique, the major impediments at present are the lack of infrastructure and the aid-induced overvaluation of the real exchange rate.

[33] Radelet, Sachs and Lee (1997) argue that *the* distinguishing feature of East Asia was the expansion of manufactured exports. A close reading of the history of that region, however, shows that agriculture provided a solid and continuing foundation for that growth (Goldman 1994; Radelet and Sachs 1998; Mellor 2000).

[34] Gallup, Radelet and Warner cite Zambia as a country where the income of the poor over the sample period has grown more than 2 percent faster than the average income of the whole population. This is a curious finding since average per capita income in Zambia has declined almost continuously since the mid-1970s.

[35] Gallup, Radelet, and Warner 1999, p.6, n.6

[36] There is now a growing literature on "coping" which emerged from an even larger literature on "safety-first." Bush (1996), Moser (1996), and World Bank (2000, Ch.4) highlight many of pressures involved and illustrate some of the strategies adopted by the poor.

[37] Whether the characterization of 'stale' is warranted or not, others will have to judge. The data cited here are among some of the most recent available on Mozambique. For policy makers, the most important issue is whether the data (even if out-dated) correctly reflect the trends in the economy. If poverty has dropped dramatically in the last year, if aid dependence has declined dramatically, and if rural welfare has improved inordinately, then the GoM can move beyond a poverty reduction and growth strategy and tackle other pressing matters. If not, appropriate measures will be needed to deal with the trends revealed by the data.

[38] More recent data from the web show that the situation has not improved. The current account deficit of the balance of payments was 34.1 percent of GDP in 1999. (Source: www.newafrica.com) The World Bank data in the update *Mozambique at a glance* show 31.7 percent.

[39] This comment appeared in the draft report. I have been informed (but do not appreciate why) that most analysts and key policy makers in Mozambique believe that any further real devaluation is "out of the question." This position owes more to politics than economics. As experience across Africa has shown, beginning with Ghana in the early 1960s, it is exceedingly dangerous for any government to decide that further real devaluation is off the agenda. For Mozambique to grow and develop rapidly, further real devaluation of the exchange rate is inevitable.

The recent debt relief and continued flow of donor support, while convenient stop-gaps, should not disguise the underlying dynamics of the economy. Imports will continue to exceed exports for the foreseeable future; and domestic output, though recovering, will remain deficient. To restore balance, further devaluation of the real exchange rate will be needed. For those interested in the mechanics the models, Johnson (1973) and Gillis *et al.* (1996:Ch.20) provide the theory.

[40] Dervis and Petri 1987; Krugman 1989; van Wijnbergen 1989; Bruno *et al.* 1991; Duesenberry and McPherson 1991, 1992; Easterly and Schmidt-Hebbel 1993; van de Walle 1994; World Bank 1994; Bouton, Jones, and Kiguel 1994; Berthelemy 1995; Easterly and Levine 1995; Goldsbrough *et al.* 1996; McKenzie *et al.* 1996; Schmidt-Hebbel 1996; Ghura and Hadjimichael 1996; Fischer, Hernandez-Cata and Khan 1998; IMF 1999, Ch.IV; Collier and Gunning 1999, 1999a; Calamitsis, Basu and Ghura 1999; Halvorson-Quevedo 2000

[41] The list of regressors CBG include is long. However, this is not a useful criterion for leaving potentially relevant variables out. Other equally important explanatory variables would be net aid flows, debt service, geographical isolation, estimates of capital flight, and primary export dependence.

[42] Whether this is purely statistical or has any economic significance is not clear. CBG did not run tests to check.

[43] This result needs to be more carefully interpreted in the light of empirical findings from a dynamic cross-country system of equations based on data from 39 African countries (McPherson and Rakovski 2000).

[44] This is clearly an area where simultaneity creates problems. Since inflation is related to the budget deficit through money creation, the variables are unlikely to have an independent effect on the growth of real income.

[45] This finding contrasts with the results of the assessment by World Bank staff of the outcome of donor-supported adjustment in Africa (World Bank 1994; Bouton, Jones and Kiguel 1994). They found that economic performance in a selected number of countries had improved even though most countries had implemented significantly fewer of the reforms than expected.

[46] World Bank 1981, 1983, 1995, p.2, 2000; Eicher 1982, 1992; Gakou 1987; Harrison 1987; Iliffe 1987; Serageldin 1989; Oyejide 1993; Lynn and Haddad 1994; Sahn 1994; Pinstrup-Anderson and Pandya-Lorch 1995; OXFAM 1995; Husain 1996; Bathrick 1998; GCA 1999; Gallup and Sachs 1999; World Bank 2000, Ch.4.

[47] I have been informed that this is not the case in Mozambique. Recent household surveys show that urban households are slightly larger than rural households. (I thank Bruce Bolnick for this point.) This result is anomalous for Africa more generally. Why? Were rural disruptions so widespread that rural relatives sent children to town for safety? Was this another form of population displacement that led more than a million Mozambicans to relocate in Malawi and Zambia? Or, has access to relief been more secure in the urban areas that household formation there has been more secure? An important question for policy makers is whether this pattern of household size is permanent. If not, a surge in rural population growth should be expected as household sizes begin to re-balance.

[48] Initial evidence in Mozambique suggests that HIV/AIDS may be higher in urban and more densely populated areas along transport routes. If so, the epidemic remains in relatively early phase. From experience elsewhere in Africa, rural debility and mortality will tend to rise over time as the epidemic spreads more generally. This will lead to an increase in the number of dependent children being raised by grandparents and older siblings.

[49] "Poor Relations: Are third world commodity producers condemned to eternal poverty?" *The Economist* 16th April, 1994, p.82

[50] *Agricultural Outlook* March 2000, Table 54. Data from the U.S. Department of Agriculture, Economic Research Service web site report data on farm productivity from 1948 onwards. Over the entire period 1948 to 1994, the growth of total factor productivity in U.S. agriculture averaged 1.94 percent per annum. The annual increase from

1948 to 1960 was 1.12 percent per annum and from 1980 to 1990, 3.36 percent. During the "productivity slow down" of the 1970s the increase was "only" 1.22 percent per annum. A more detailed study of the source of agricultural growth in the U.S. is available in Eldon Ball *et al.* (1997).

[51] Smith (1789, Skinner edition 1979, p.121):

> As it is the power of exchanging that gives occasion to the division of labour, so the extent of that division must always be limited by the extent of that power, or, in other words, by the extent of the market.

[52] The World Bank went part of the way in its study of economic reform in Africa (World Bank 1994) and the follow up (Bouton, Jones and Kiguel 1994). Both studies confirm the more general point that all African countries have promised far more than they have delivered in terms of reform. There are many reasons for this – local politics, the dynamics of aid, poor economic management, and so on. Whatever the cause, any solution must involve a drastic scaling back of the development agenda so that governments have a reasonable chance of delivering what they promise. There is now considerable experience how this might be done based on the structural adjustment programs undertaken in Asia (Lindauer and Roemer 1994; Perkins 1994) and selected developed countries (OECD 1994; Evans *et al.* 1996). In developing countries, it is common to attribute slow reform to political difficulties. In this regard, the example of Sweden (one of Africa's most generous and least demanding donors) should put that matter to rest. Sweden cut its budget deficit from 16 percent of GDP in 1993 to less than 1 percent in 1997 and generated a surplus in 1998 (Source: *IFS* November 1999). No African country has implemented such a dramatic change and sustained it. To presume Sweden had fewer political difficulties because it is 'rich' misses the point.

[53] I note, however, with some degree of pleasure that the Horst Köhler, the recently appointed Managing Director of the IMF, indicated that he believed developing countries were attempting to tackle too many problems at once (*The Economist* 29th July, 2000, p.66). I look forward to the day when his views become the norm throughout Africa.

[54] Bloom and Gallup (1997) suggest that, at a broader level, there is not much convincing evidence that expenditures at higher levels of government are associated with poverty reduction.

[55] The World Bank (1997) defined environmental health as:

> …[T]he body of knowledge concerned with the prevention of disease through control of biological, chemical, or physical agents in the air, water, and food, and the control of environmental factors which may have an impact on the well-being of people.

[56] This point is supported through a case study and general literature review of the experience of Southern Africa (Hoover and McPherson 1999, 2000; McPherson, Hoover, and Snodgrass 2000). Some recent innovative approaches to adult education that have relevance in this area are summarized by Breth (2000).

[57] Simon, Rosen, and Whitehead (2000) note that many businesses have been outsourcing services they used to provide themselves. At the micro level, this transfers the costs of the high incidence of HIV/AIDS to sub-contractors. At the macro level, it reduces the overall efficiency of the economy, especially when all firms try to shift costs.

[58] There is now a growing literature dealing with ways of exiting from aid (Fernholz *et al.* 1996; Berg 1996; HIID 1997; McPherson 1999; McPherson and Gray 2000). The closest the World Bank comes is in the final pages of its latest report on Africa (World Bank 2000a, pp.256-258) where it mentions the need to move "away from aid dependence." No specifics are given on how that might be achieved or over what time period.

[59] Johnson (1997) reported the performance of countries that have been receiving aid from the United States for periods of up to 50 years. In some countries (most of which are in Africa), real per capita income has declined.

[60] Net assistance flows were around 3 percent of GDP in the early 1970s rising to a peak of 15.4 percent in 1995. They subsequently declined to around 12.5 percent in 1998. The data are from the *World Development Indicators* 1999, CD-ROM assembled by the World Bank.

[61] Lancaster (1999) made an important attempt to examine the merits and demerits of aid. She finds that foreign aid has been far less effective than the principal donors are comfortable acknowledging.

[62] Financial analysts regularly deal with issues of adverse selection and moral hazard. Both apply in the aid business. Adverse selection is evident in the fact that the worst performing countries attract more aid over longer periods than countries whose performance improves. (Mauritius is an obvious African example.) Moral hazard is evident in the problems that arise when governments receive aid as a means of inducing better performance. Some governments (Kenya and Senegal were highly adept at this) have managed to perform not quite as well as expected without losing the support of the donor community.

[63] Ramakrishnan (1998) reviews the problems of budgeting systems in Africa. Goldbrough *et al.* (1996) review several case studies illustrating these problems as well.

[64] Reviewing the lessons of the Mexican crisis, Summers (1995) noted:

> …[S]ound policies are absolutely essential. One of the most foolish things said about the international economy these days is that because capital moves so quickly and so freely, government policies have little influence. In reality, precisely because of greatly increased capital mobility, the difference between having the right and the wrong government policies has never been greater.

[65] The argument that globalization has 'gone too far' (Rodrik 1997) is beside the point for a country such as Mozambique. Under present and foreseeable circumstances, Mozambique's economic future is non-viable unless policy makers take the greatest advantage of the opportunities provided by the internationalization of economic activity.

[66] Collier and Gunning (1999) report research by the World Bank showing that average returns on investment in Africa were higher than in other regions. However, they argue in a subsequent paper (1999a) that the risk-adjusted returns to investment in Africa has been low.

[67] This has been the strategy followed by both Botswana and Mauritius.

[68] World Bank News Release No: 2000/297/S "Mozambique qualifies for an additional US $600 million in debt relief under enhanced HIPC initiative, bringing its total debt reduction to US $4.3 billion." Located on www.wbln0018.worldbank.org/news.

[69] Unit labor costs are productivity-adjusted wages measured in foreign exchange. Low unit wage costs are essential for a country to realize its dynamic comparative advantage (Bruno 1972; Mead 1990; Lindauer and Valenchik 1994).

[70] Ndulo and Ndung'u (1997) addresses many of the same questions about the links between trade and growth. For reasons not stated in their study, Ndulo and Ndung'u specified their equations in a way that excluded all simultaneous effects between the two.

[71] Although most African governments lost the habit, responsible fiscal policy should aim for a balanced budget. With Mozambique currently undergoing an aid-induced boom, the budget should be in surplus. Since Mozambique has a large debt burden (even after HIPC-II relief), a sustainable balance of payments deficit will be equivalent to the proportion of GDP consisting of permanent aid flows plus private equity and remittances.

[72] Such an anticipated response has been the rationale for structural adjustment (IMF 1987; McKenzie *et al.* 1996; Calamitsis, Basu and Ghura 1999).

[73] McPherson (1995) reviews this literature.

[74] The problem with the view that sequences can be optimally determined is the 'Lucas critique' (Lucas 1976). Since economic reform is designed to change the structure of an economy, it is logically impossible to optimally sequence reforms in advance. The pattern of reform actually achieved in any economy is path dependent.

[75] The implications of this issue for agriculture have been examined by (among others) Binswanger and Deininger (1997), Schiff and Valdes (1998), and Barrett and Carter (1999). Snowdon and Vane (1997) consider it within the context of the broader economy.

[76] A similar problem has emerged in transition economies. Havrylyshyn and Olding-Smee (2000) interpret the problem of stalled reforms and weak responses as reflecting the willingness of vested interests to block reforms. Mellor (2000) interpreted the slowing of agricultural growth in Asia from the mid-1980s onward in the same terms.

[77] Even ascetics can be costly. Mahatma Gandhi is a well-known example. One of his benefactors lamented: "If only Bapu [Gandhi] knew the cost of setting him up in poverty!" (Sherrin 1995, p.258).

[78] Yeats (1994) casts doubt on the usefulness of African trade data. Various references, however, show that intra-African trade flows have been low (Hardy 1992; *Economist* 5 March 1994; Stryker, Salinger and Barry 1996; *African Development Indicators* 1998/99:Tables 5.47 to 5.55; Luvanga and Bol 1999:Table 5).

[79] Radelet (1997) has other examples.

[80] Drought has been a serious recurrent problem across most of Africa for the last three decades (Glantz 1989; World Bank 1996; Bensen and Clay 1998). A major problem, however, is that few African governments take drought (and similar disturbances) into their financial programming.

[81] Rising water use in Botswana and Namibia and the increasing aridity in Zimbabwe (especially around Bulawayo) will increase the rate of extraction from the Zambezi River. Over the longer term, South Africa has indicated that it will seek access to the Zambezi to supply some of its northern areas. Without major works that divert the Luapula down the Kafue River, future average flows to Mozambique will decline. As noted in the text, the whole question of water supply and water use will demand much more attention than is currently being devoted to the issue (World Bank 1996; Rosen and Vincent 1999).

[82] Some major progress has been made in critical areas of agricultural production (Schioler 1998). But, for progress to continue, research on these issues needs to be strengthened. Some of the major topics include methods to enhance livestock production, the prevention of land degradation, the use of biotechnology to improve drought and disease resistance, pest management, support for the development of rural markets, water management, and the promotion of rural support services (ICRISAT 1985; Harrison 1987; WINROCK 1993; Stryker and Shaw 1994; Abassa 1995; IFPRI 1995; World Bank 1996, 1998; Scherr and Yadav 1997; Conway 2000; *Economist* 2000).

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